LIBRARY
SUPREME COURT. U. S.

Office - Supreme Court, U.S.
FILED
FEB 21 1958
[illegible], Clerk

IN THE

Supreme Court of the United States

OCTOBER TERM, 1957.

No. 801

G. W. THOMAS DRAYAGE & RIGGING COMPANY, INC., a corporation, W. R. BALLINGER & SON, a corporation, and MINNA M. BALLINGER,

Petitioners,

vs.

INDUSTRIAL INDEMNITY COMPANY, a corporation; INDUSTRIAL INDEMNITY EXCHANGE, a reciprocal exchange; T. G. McGUIRE, E. A. MATHIESSEN, S. E. HODAPP, J. V. CHAMBERS, M. S. FIELDS, E. E. URSIN, D. W. SCHIEBEL, W. A. HALUK, R. E. MAY, JR., R. L. JONES, JR., FRED DREXLER, N. S. YOUNG, THOMAS SOULE, J. P. TAHENY and V. E. HOWARD, JR., doing business as Industrial Service Company, a copartnership, HENRY J. KAISER, K. K. BECHTEL, S. D. BECHTEL, JOHN A. McCONE, W. A. BECHTEL, JR., T. G. McGUIRE, E. S. DULIN, F. SOMERS PETERSON, JAMES M. SMITH, M. I. SMITH, ALDEN G. ROACH, ROBERT L. BRIDGES, H. S. LORD, A. F. BISHOP, all of the aforesaid doing business as INDUSTRIAL UNDERWRITERS, a partnership, K. K. BECHTEL, L. T. KETT, F. SOMERS PETERSON, J. W. SCAMMELL, G. G. SHERWOOD, EMERSON SPEAR, A. G. STREBLOW, G. J. THOMPSON, W. E. WASTE, JOSHUA HENRY IRON WORKS, a corporation, INTERNATIONAL ENGINEERING COMPANY, INC., a corporation, and MARINE TERMINALS CORPORATION, a corporation,

Respondents.

Petition for a Writ of Certiorari to the Supreme Court of the State of California.

ROBERT W. KENNY,
FRANK B. BELCHER,
1557 Beverly Blvd.,
Los Angeles 26, California,
Attorneys for Petitioners.

BELCHER, KEARNEY & FARGO,
KENNY & MORRIS,
JEROME POLITZER,
MORRIS E. COHN,
HYMAN & HYMAN,
Of Counsel.

Parker & Son, Inc., Law Printers, Los Angeles. Phone MA. 6-9171.

SUBJECT INDEX

PAGE

Opinions below 2

Jurisdiction 3

Questions presented 3

Constitutional and statutory provisions involved..... 4

Statement of the case..... 5

How federal questions are presented..... 14

Reasons for granting the writ..... 18

Conclusion 35

INDEX TO APPENDICES

Appendix A. Opinion of the Supreme Court (49 A. C. 257, 316 P. 2d 966).

Appendix B. Opinion of the District Court of Appeal (117 Cal. App. 2d 519, 256 P. 2d 677).

Appendix C. Opinion of the District Court of Appeal (144 A. C. A. 244, 301 P. 2d 112).

TABLE OF AUTHORITIES CITED

CASES	PAGE
Brinkerhoff Faris Trust & Savings Company v. Hill, 281 U. S. 673	32, 34
Buchanan v. Warley, 245 U. S. 60	19
Cain v. Burns, 131 Cal. App. 2d 439, 280 P. 2d 888	31
Carter v. Seaboard Finance Co., 33 Cal. 2d 564, 203 P. 2d 758	31
Chicago, Burlington and Quincy R.R. Co. v. Chicago, 166 U. S. 226	18
Chicago, M. & St. P. Ry. Co. v. Des Moines Union Ry. Co., 254 U. S. 196	25
Chicago, Milwaukee and St. Paul R.R. Co. v. Wisconsin, 238 U. S. 491	19
Citizen's National Bank v. Appleton, 216 U. S. 196	26
Corsicana National Bank v. Johnson, 251 U. S. 68	26
Deacon v. Bryans, 212 Cal. 87, 298 Pac. 30	33
Fiske v. Kansas, 274 U. S. 380	35
Gatti v. Highland Park Builders, 27 Cal. 2d 687, 166 P. 2d 265	31
Gore v. Bingaman, 20 Cal. 2d 118, 124 P. 2d 17	33
Hill v. Maryland Cas. Co., 28 Cal. App. 422, 152 Pac. 953	33
Holden v. Hardy, 169 U. S. 366	19
Hoopeston Canning Co. v. Cullen, 318 U. S. 313	5, 20
Hoover & Allison Co. v. Evatt, 324 U. S. 652	35
Huber v. Martin, 127 Wis. 412, 105 N. W. 1031	5, 20
Jackson v. Ludeling, 88 U. S. 616	25
Koehler v. Black River Falls Iron Co., 2 Black (U. S.) 715	25
Magruder v. Drury, 235 U. S. 106	26
Manufacturing Lumbermen's Underwriters, In re, 18 Fed. Supp. 114	20
McGourkey v. Toledo and Ohio Cent. Ry. Co., 146 U. S. 536	25
Michoud v. Girod, 4 How. (U. S.) 502	24
Missouri v. Gehner, 281 U. S. 313	34

PAGE

Missouri Pacific Railway v. Nebraska, 164 U. S. 403 19
Mosser v. Darrow, 341 U. S. 267 26
Norris v. Alabama, 294 U. S. 587 35
Norwood v. Judd, 93 Cal. App. 2d 276, 209 P. 2d 24 31
Oyama v. California, 332 U. S. 633 35
Poultry Producers, etc. v. Barlow, 189 Cal. 278, 208 Pac. 93 31
Reagan v. Farmers Loan and Trust Co., 154 U. S. 362 31
Robertson v. Hyde, 58 Cal. App. 2d 667, 137 P. 2d 703 31
Saunders v. Shaw, 244 U. S. 317 34
Savings Bank of San Diego County v. Burns, 104 Cal. 473, 38 Pac. 102 31
Shelley v. Kraemer, 334 U. S. 1 32
Stock v. Meek, 114 Cal. App. 2d 584, 250 P. 2d 622 33
Thompson v. Consolidated Gas Utilities Corp., 300 U. S. 55 18
Treigle v. Acme Homestead Association, 297 U. S. 189 18
Truax v. Raich, 239 U. S. 33 32
Tyson and Brother v. Banton, 273 U. S. 418 19
United Dredging Co. v. Indus. Acc. Comm., 208 Cal. 705, 294 Pac. 922 33
Wardell v. Railroad Co., 103 U. S. 651 25
Weichman v. Vetri, 113 Cal. App. 2d 717, 248 P. 2d 783 33
Westinghouse Electric and Mfg. Co. v. Wagner Electric and Mfg. Co., 225 U. S. 604 25
Wilson v. Marshall, 218 S. W. 2d 345 20
Yick Wo v. Hopkins, 118 U. S. 356 32

STATUTES

California Insurance Code, Sec. 1101 .... 4, 8, 9, 15, 16, 21, 28, 31
California Insurance Code, Sec. 1106 ..... 5, 8, 21
California Insurance Code, Sec. 1282 5
United States Code, Title 28, Sec. 1257(3) 3
United States Constitution, Fourteenth Amendment 4, 19, 31, 32

MISCELLANEOUS PAGE

94 American Law Reports, p. 836 20
141 American Law Reports, p. 765 20
145 American Law Reports, p. 1121 20
18 Appleman, Insurance Law and Practice (1945), Sec. 10121 et seq. 5
4 California Jurisprudence 2d, Sec. 691, p. 598 33
Restatement of Law of Agency, Sec. 403 26
Restatement of Law of Agency, Sec. 404 26
Restatement of Law of Agency, Sec. 407 26
Restatement of Law of Restitution, Sec. 160(d) 26
Restatement of Law of Restitution, Sec. 202(c) 26
Restatement of Law of Trusts, Sec. 202 26
Restatement of Law of Trusts, Sec. 203 26
Restatement of Law of Trusts, Sec. 205 26
Temporary National Economic Committee (76th Cong.), Monograph 28 5
Vinter, Treatise on the History and Law of Fiduciary Relationship and Resulting Trusts (Cambridge, 1955), 3rd Ed., p. 145 24

IN THE

Supreme Court of the United States

OCTOBER TERM, 1957.

No. .....

G. W. THOMAS DRAYAGE & RIGGING COMPANY, INC., a corporation, W. R. BALLINGER & SON, a corporation, and MINNA M. BALLINGER,

Petitioners,

vs.

INDUSTRIAL INDEMNITY COMPANY, a corporation; INDUSTRIAL INDEMNITY EXCHANGE, a reciprocal exchange; T. G. McGUIRE, E. A. MATHIESSEN, S. E. HODAPP, J. V. CHAMBERS, M. S. FIELDS, E. E. URSIN, D. W. SCHIEBEL, W. A. HALUK, R. E. MAY, JR., R. L. JONES, JR., FRED DREXLER, N. S. YOUNG, THOMAS SOULE, J. P. TAHENY and V. E. HOWARD, JR., doing business as Industrial Service Company, a copartnership, HENRY J. KAISER, K. K. BECHTEL, S. D. BECHTEL, JOHN A. McCONE, W. A. BECHTEL, JR., T. G. McGUIRE, E. S. DULIN, F. SOMERS PETERSON, JAMES M. SMITH, M. I. SMITH, ALDEN G. ROACH, ROBERT L. BRIDGES, H. S. LORD, A. F. BISHOP, all of the aforesaid doing business as INDUSTRIAL UNDERWRITERS, a partnership, K. K. BECHTEL, L. T. KETT, F. SOMERS PETERSON, J. W. SCAMMELL, G. G. SHERWOOD, EMERSON SPEAR, A. G. STREBLOW, G. J. THOMPSON, W. E. WASTE, JOSHUA HENRY IRON WORKS, a corporation, INTERNATIONAL ENGINEERING COMPANY, INC., a corporation, and MARINE TERMINALS CORPORATION, a corporation,

Respondents.

Petition for a Writ of Certiorari to the Supreme Court of the State of California.

Petitioners pray that a writ of certiorari issue to review the judgment of the Supreme Court of the State of California affirming a judgment rendered by a Judge of the Superior Court of the City and County of San Francisco determining the nature, extent and value of the business,

property and assets of a reciprocal insurance association illegally obtained by respondents, following a decision by the District Court of Appeal, First Appellate District, Division Two, State of California, reversing the aforesaid judgment of the Superior Court upon the principal ground that the judgment operated arbitrarily and unlawfully to deprive the subscribers of the said reciprocal insurance association of their property, privileges and interests therein with a resultant substantial and wrongful windfall to respondents in a sum exceeding five million dollars.

Opinions Below.

No written opinion was rendered by the Judge of the Superior Court who presided at the first trial of the cause herein. On the first appeal, a written opinion was rendered by the aforesaid District Court of Appeal, reported in 117 Cal. App. 2d 519, 256 P. 2d 677, and set forth in Appendix B to this petition. No opinion was rendered by the District Court of Appeal in thereafter denying a petition for a rehearing, or by the Supreme Court in denying a petition for a hearing (117 Cal. App. 2d 541).

No written opinion was rendered by the Judge of the Superior Court who presided at the second trial of the cause herein. On the second appeal, a written opinion was rendered by the same District Court of Appeal, reported in 144 A. C. A. 244, 301 P. 2d 112, and set forth in Appendix C to this petition. The opinion of the Supreme Court, three Justices dissenting, is reported in 49 A. C. 257, 316 P. 2d 966, and set forth in Appendix A to this petition. No opinion was rendered by the Supreme Court in denying the petition for rehearing, except that Mr. Chief Justice Gibson, Mr. Justice Carter and Mr. Justice Traynor were of the opinion that the petition should be granted.

Jurisdiction.

The judgment of the Supreme Court was made and entered on October 30, 1957 (App. A). A timely petition for rehearing was filed in the Supreme Court and denied on November 26, 1957, Mr. Chief Justice Gibson, Mr. Justice Carter and Mr. Justice Traynor being of the opinion that the petition should be granted. The jurisdiction of this Court is invoked under 28 U. S. C. 1257(3) in that petitioners' titles, rights and privileges were specially set up and claimed under the Fourteenth Amendment to the Constitution of the United States.

Questions Presented.

In express violation of statute and fiduciary duty, the attorney-in-fact of the reciprocal insurance exchange herein transferred the business and assets of the exchange to a competing company, whose stock ownership was substantially the same as that of the attorney-in-fact. The state courts had decreed in 1953 that the business and assets of the exchange, or the value thereof, should be returned to exchange and its subscribers, the petitioners here as representatives of the class. However, the judgment below denied restitution to exchange and its subscribers of the *profits* made by the competing company, *after* the transfer, directly traceable to the former clients of the exchange. The judgment also denied restitution of all the investment earnings of exchange which passed into the hands of the company after the invalid transfer. Exchange and its subscribers were also charged with fees for services rendered by the company to the former clients of exchange after the wrongful transfer. The total of these three items exceeds $5,000,000 and the judgment in effect denied restitution of this sum to the exchange and its subscribers although it was retained by respondents as a result of the unlawful transfer of claimed business and assets.

The questions presented are:

1. Whether the judgment of the court below operated to deprive petitioners of their property, rights and interests in the said reciprocal insurance exchange arbitrarily and capriciously and without due process of law in violation of the due process provisions of the Fourteenth Amendment to the Constitution of the United States.

2. Whether the judgment of the court below operated arbitrarily, capriciously and discriminatorily to deprive petitioners of their property, rights and interests in the said reciprocal insurance exchange and thus denied petitioners the equal protection of the laws in violation of the equal protection provisions of the Fourteenth Amendment to the Constitution of the United States.

Constitutional and Statutory Provisions Involved.

1. Constitution of the United States, Fourteenth Amendment:

> ". . . Nor shall any State deprive any person of life, liberty, or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws."

2. California Insurance Code, Section 1101:

> *"Personal interest of officers or employees; exceptions Personal interest.* An admitted insurer's officers, directors, trustees and any persons who have authority in the management of the insurance funds, shall not, unless otherwise provided in this code:
>
> * * * * * * * *
>
> "(c) *Purchase of assets.*
>
> "Directly or indirectly purchase, or be interested in the purchase of, any of the assets of the insurer."

3. California Insurance Code, Section 1106.

"Any person violating . . . Sections 1101 . . . is guilty of a misdemeanor."

4. California Insurance Code, Section 1282.

"The provisions of the following sections, articles and chapters shall be applicable to reciprocal or interinsurance exchanges:

* * * * * * * *

"Sections 1101 to 1106, inclusive;

* * * * * * * *

Statement of the Case.

1. The Industrial Indemnity Exchange, hereinafter referred to as Exchange, is a reciprocal insurance association under which subscribers acting by and through their attorney-in-fact exchange insurance contracts with one another providing workmen's compensation and employers' liability insurance.[1]

The petitioners are subscribers of Exchange and they appear in these proceedings in a representative capacity on

---

[1]The nature of the business of Exchange, its history and its interrelations with the different respondents are fully discussed in the opinions of the courts below. See Appendix A, pp. 259-61; Appendix B, pp. 522-26; Appendix C, pp. 246-48. So much of the facts which are material to the consideration of the questions presented herein are set forth in this Statement of the Case. For a discussion of some constitutional and legal aspects affecting reciprocal insurance associations, see *Hoopeston Canning Co. v. Cullen,* 318 U. S. 313; *Huber v. Martin,* 127 Wis. 412, 105 N. W. 1031. For a general discussion, see Appleman, *Insurance Law and Practice* (1945), Vol. 18, Section 10121 *et seq.* For a discussion of the financial abuses in the field by controlling officers, and the impact on the national economy, see *Temporary National Economic Committee* (76th Cong.), Monograph 28.

behalf of all persons who were subscribers at and had policies in force with Exchange on December 31, 1948 [R. 65].[2]

Each and every subscriber to Exchange executed an Underwriters Agreement containing powers of attorney [Deft. Ex. 6, R. 244]. In said underwriters agreements the subscribers to Exchange designated an attorney-in-fact with power to make and exchange insurance contracts with the other subscribers. In all of said underwriters agreements, Industrial Underwriters, a partnership, hereinafter referred to as Attorney was designated as attorney-in-fact.

Industrial Indemnity Company, hereinafter referred to as Company, is engaged in the competing business of writing workmen's compensation and employers' liability insurance as a stock insurance company.

It is not in dispute that the stock ownership of Company has at all times been substantially the same as the ownership of Attorney, the attorney-in-fact for the subscribers to Exchange (App. A, p. 260; App. B, p. 522; App. C, p. 246).

2. For some time prior to 1947, Attorney and Company engaged in a series of transactions which plainly evidenced a breach of fiduciary duties to the subscribers of Exchange, and a diversion of the business and assets of Exchange to Company (App. B, pp. 523-526). The interrelations and interlocking functions of Attorney and Company which were causing a waste of the assets of Exchange and the siphoning away of its business came under the critical examination of the Insurance Commissioner of

---

[2]The reference "R" is to the pages of the certified record filed herein with this petition.

the State of California (App. B, pp. 523-524). Negotiations thereupon ensued between Attorney, Company and the Insurance Commissioner (App. B, pp. 523-526). The outcome of these negotiations was the approval by the Insurance Commissioner of a plan suggested by Attorney and Company whereby all the business and assets of Exchange were sold to Company as of December 31, 1948. Company agreed to pay to the subscribers of Exchange an amount equal to the entire net worth of Exchange. The agreement was in writing, entitled Transfer and Assumption Agreement [Pltf. Ex. 14, R. 468; App. A, pp. 282-284]. A three-year period was permitted to ascertain the adjusted net worth of Exchange (1949-1951), it being agreed that Company would pay $1,000,000 on or before March 31, 1949; $500,000 on or before March 31, 1950; and any balance remaining due, on or before March 31, 1952 (App. A, p. 284). The agreed purchase price, or the adjusted net worth of Exchange, as of December 31, 1951, turned out to be $1,018,589.07, computed in accordance with the agreement (App. C, p. 251).

3. Court approval was now sought for the aforesaid agreement. Company, Attorney, Exchange, consenting subscribers and the interlocking individual owners joined as plaintiffs in a declaratory relief action seeking judicial confirmation of the agreement. In short, the respondents here were the plaintiffs below. The non-consenting subscribers, the petitioners here, were the defendants and cross-complainants below (App. B, p. 522).

So far as is pertinent here the position of respondents at the first trial in the Superior Court was simply that the agreement of sale of Exchange to Company was in all respects fair and equitable, and that the purchase price to be distributed to the subscribers, estimated at the first trial

to be $1,894,347.07, properly represented the net worth of Exchange.

The position of petitioners was (1) that the agreement was invalid as a fraudulent attempt by Attorney to eliminate Exchange as a competitor of Company; (2) that the subscribers were entitled, in addition to the agreed purchase price, to the value of the business of Company built up unlawfully by Attorney and Company at the expense of Exchange; and (3) that the subscribers were in any event, in addition to the agreed purchase price, entitled to the value of the goodwill of Exchange (App. B, p. 525).

The judgment of the Superior Court was substantially for the respondents. The agreement and purchase price were held valid; it was decided that the subscribers were entitled to nothing further (App. B, p. 526).

4. An appeal was now prosecuted to the District Court of Appeal. It should be noted in the posture of that appeal that the trial court had concluded that the net worth of Exchange was properly fixed at an estimated $1,894,-347.07; that respondents also urged that this agreed price was in all respects fair; and that petitioners, who were appealing, argued that this minimal figure should be necessarily increased by millions of dollars.

On appeal, the case took a different turn. The District Court of Appeal, on its own motion, held that the transfer and assumption agreement between Attorney, Company and Exchange was void as violating Section 1101 of the California Insurance Code. That section makes it illegal for any officer of an insurer to directly or indirectly purchase any of the assets of the insurer. Another section of the Insurance Code (1106) makes it a misdemeanor to participate in any such purchase. Since it was undisputed that the stock ownership of Company and the ownership

of Company and the ownership of Attorney were the same (App. B, p. 527), it followed that the statute had been clearly violated.

It is important in connection with these proceedings to note the argument made by respondents in support of the legality of the agreement. Respondents contended that the agreement was not a beneficial sale of assets to Company as prohibited by Section 1101 aforesaid, but a transfer for the purpose of liquidation only. To this argument, the District Court of Appeal stated: "We do not agree" (App. B, p. 528). The Court held that the undisputed documentary proof established that Company was a purchaser, and not a liquidator, of Exchange (App. B, pp. 528-529). It held further as follows:

> "By taking over all assets, assuming all liabilities, including all outstanding policies of Exchange and becoming directly liable thereon to the policyholders, the Company acquired the whole business of the Exchange as a going concern and would therefore benefit by the increase of its clientele" (App. B, p. 529).

Having found the agreement unlawful, the District Court then turned to the cross-complaints of petitioners. As to the claim by the subscribers to the business of Company, this claim was denied (App. B, pp. 533-535). As to the claim by the subscribers to the value of the goodwill of Exchange, this claim was upheld—"they have a right to the business taken over by Company in consequence of the transfer and assumption agreement, which we have held to be invalid" (App. B, p. 539). The judgment was thereupon reversed with directions to grant such relief to petitioners on their cross-complaints as would

> "enable them to recover in their representative capacity for subscribers the business and assets obtained

by Company in consequence of the agreement herein held to be invalid, and to wind up fully all matters relating thereto" (App. B, pp. 540-541).

5. Respondents did not file a petition for hearing to the Supreme Court following the aforesaid decision of the District Court of Appeal. An intervening party did file such petition, and respondents in answer to said petition explained that they had filed no petition for hearing on their own behalf because under the decision of the District Court of Appeal, Company would pay and the subscribers of Exchange would receive amounts or assets having the same value as under the transfer and assumption agreement, a position which Company took throughout these proceedings [R. p. 707; App. A, p. 275]—the respondents however maintaining in their answer to the petition for hearing that the agreement was one for liquidation and not of purchase as the District Court had held. The petition for hearing was denied and the legal principles applicable to the case thereupon became fixed.

6. By the time the second trial began (December, 1954), it was possible to calculate accurately what would have been received by the subscribers under the transfer and assumption agreement. That sum was $1,018,589.07 [R. p. 67], instead of the $1,894,347.07, estimated at the time of the first trial.

(a) In accordance with the judgment of the District Court of Appeal, petitioners undertook to establish to how much more they were entitled. Since five years had passed after the sale of Exchange to Company, it was possible for petitioners to avoid speculation as to the going concern value of Exchange and to trace directly the business obtained by Company from the clientele of Exchange. This item was estimated at $1,609,960 as of March 31, 1954,

for business done in the policy years 1949, 1950, 1951 and 1952 [R. p. 89 *et seq.;* see Condensed Summary at p. 5 of actuary's report accompanying Deft. Ex. 3]. It was estimated that the profits to be derived from policies to be written in 1953 and thereafter for former policyholders would be $2,656,740 [see Condensed Summary, *supra*].

The trial court denied the claim *in toto*. Essentially it held that since the evidence showed that policies were renewed annually, there was no assurance that Exchange would have had any future policyholders had it not been put out of business [R. p. 73]; this despite the undisputed testimony that the clientele of Exchange had been taken over by the illegal sale of Exchange to Company in 1948, that the business obtained from such clientele would amount to over $4,000,000, and that the binding judgment of the District Court required restitution to the subscribers of the value of the business thus obtained.

(b) If the trial court disregarded the judgment of the District Court in the aforesaid respect, it may be presumed that the court would at least have returned to the subscribers of Exchange the net worth of Exchange which had never been in question, the sum of $1,018,589.07. This was not done. Instead the trial court charged off a series of amounts against this minimal sum which resulted in effect in handing over the assets of Exchange to Company, after Company had been directed to return these assets or the value thereof to Exchange.

Thus, initially, the respondents were credited with $156,600.51 because they lost that much in servicing the 1949 portion of the Exchange policies of the policy year 1949, the partial first year of the illegal operation which had been specifically condemned. This should be contrasted with the refusal to grant the subscribers of Exchange any

amount for the business wrongfully obtained by Company in the years 1949 and thereafter.

(c) One of the important assets of Exchange were its investment earnings. Under the underwriters agreement prior to 1948, these earnings were set aside in a Special Surplus Fund to be used for the expenses of liquidation in the event Exchange was ever liquidated by Attorney in accordance with the terms of the underwriters agreement. That this fund was an asset of Exchange cannot be disputed. Indeed, in the transfer and assumption agreement, the Special Surplus Fund was one of the items which Company set up as an asset of Exchange (App. A, p. 301). At the time of the trial, that fund amounted to $592,-322.31 [R. p. 71]. The trial court awarded the entire sum to Company upon the ground that Attorney in 1953 had assigned the fund to Company for work performed in liquidating Exchange after the illegal transfer on December 31, 1948 [R. pp. 71-72]. Thus, despite the express holding of the District Court of Appeal that Exchange had been sold in 1948 as a going business and not for liquidation, despite the undisputed documentary proof to that effect, and despite the fact that whatever Company did with Exchange after 1948 was plainly illegal, Company was permitted to retain all the investment earnings of Exchange in payment for a liquidation which never took place.

(d) Prior to 1948, Attorney under the underwriters agreement was entitled to retain 25 per cent of the premium deposits and 5 per cent of dividends as its fee [Deft. Ex. 6, R. p. 244]. This fee was in payment for the offices, equipment and personnel used for the business of Exchange. After the sale on December 31, 1948, Company admittedly handled all the business which came in from

former policyholders of Exchange for the account of Company. Nevertheless, the trial court permitted Company to charge Exchange for the fees based on premiums collected and dividends paid after December 31, 1948, in the sum of $324,751.07 [R. p. 70].

(e) The short of the matter is that the trial court denied petitioners any amount representing the value of the going business admittedly illegally obtained by Company, and instead of even returning to the subscribers of Exchange the stipulated net worth of $1,018,589.07, the court restored to the subscribers only the sum of $323,-300.39 [R. p. 87]. The Company thus retained a substantial portion of the property and assets of Exchange as well as all the fruits of the business of Exchange, this despite the express holding of the District Court of Appeal (left undisturbed by the Supreme Court on petition for hearing) that the business and assets of Exchange had been obtained by Company in violation of the statutes of California.

7. An appeal was again prosecuted by respondents to the District Court of Appeal. That court held that its prior decision and judgment in the case had been plainly disregarded by the trial court (App. C). The Appellate Court held again that Exchange had been purchased by Company as a going business, and not for liquidation purposes only (App. C, p. 251). The court held again that Company could not retain the profits which it secured from the former subscribers of Exchange following its wrongful acquisition of the business of Exchange in breach of its fiduciary duties and in violation of the statute (App. C, pp. 253-257). The court held that the subscribers of Exchange were plainly entitled to the Special Surplus Fund, representing the investment earnings of

Exchange. The record showed without dispute that neither Attorney nor Company after 1948 were acting under the underwriters agreement. They were acting under the illegal transfer and assumption agreement and as owners of Exchange after 1948 when they attempted the unlawful liquidation of Exchange. The investment earnings of Exchange could not be used for such illegal purpose, and the subscribers were entitled to the return of the earnings as an asset of Exchange (App. C, pp. 257-259). For like reasons, the court also held that the subscribers of Exchange could not be charged with fees for services rendered by Company after 1948, since after that date Company was handling all the business for its own account (App. C, pp. 259-260).

The judgment of the trial court was reversed (App. C, p. 263). The District Court of Appeal reaffirmed the law of the case established by its prior decision—Exchange had been sold unlawfully by the fiduciary in breach of trust and in violation of statute law; the subscribers of Exchange were entitled to the entire net worth of the assets of Exchange together with the net profits resulting from the business of Exchange so unlawfully obtained by Company.

How Federal Questions Are Presented.

Following the decision of the District Court of Appeal, the respondents petitioned for hearing in the Supreme Court which was granted. Before the Supreme Court, it should be observed, the respondents were in the position of appellants; the petitioners here were in the position of appellees. This was not an ordinary appeal initially taken from a trial court directly to the Supreme Court of the State, without any prior ruling to foreshadow the eventual result. An intermediate appellate court had ruled in

favor of petitioners and fixed the applicable rules of law; a petition for hearing had been denied by the Supreme Court; and thereafter the same intermediate appellate court had again reaffirmed the same principles and given judgment for petitioners in accordance with those principles.

It could not be expected at this stage of the proceedings that the Supreme Court would disregard the rules of law fixed in the very case by the Supreme Court itself in denying a hearing on the first appeal and by the District Court of Appeal on two occasions. Questions of importance were still open in the case: whether petitioners' methods of calculating the value of the going business of Exchange was correct (App. C, p. 257); whether the trial court might reserve the right by supplemental judgments to award future profits as they actually accrued (App. C, p. 257); and whether interest was properly allowable on the awards to petitioners (App. C, p. 261). But the right of petitioners to the restitution of the assets and business of Exchange unlawfully obtained by Company appeared entirely settled in view of the rulings of the District Court of Appeal and the denial of hearing by the Supreme Court.

The decision of the Supreme Court was therefore a complete surprise and unexpected, and one which could not be reasonably contemplated. Mr. Justice Carter, dissenting, repeatedly notes that the law of the case was arbitrarily disregarded (App. A, pp. 282, 290, 294, 298). In addition, the majority decision reveals the unexpected nature of the result. For on the one hand the majority accept as established law in the case that Exchange had wrongfully been sold to Company in violation of Section 1101 of the California Insurance Code (App. A, p. 260); yet on the other hand, the decision upholds the findings that Com-

pany acted solely as liquidator of Exchange and not as the purchaser of a going business (App. A, p. 261), thus disregarding the law in the same case, twice decided by the District Court of Appeal and on which the Supreme Court had previously denied a hearing.

Moreover, it could not be expected that the Supreme Court would suddenly decide that the transfer of Exchange was for liquidation purposes only, when that would mean that Section 1101 of the California Insurance Code was not applicable to the transfer and assumption agreement (App. B, p. 528); the agreement would, therefore, not be void and the stipulated purchase price of $1,018,-539.07 would at least be the obligation of respondents.

What the majority of the court did was to arbitrarily disregard the "undisputed facts" (App. A, p. 277) in the case; and arbitrarily disregard the law of the case previously confirmed by the court; treat the illegal transfer as a liquidation, but decline to enforce the price stipulated between the parties on the basis of such transfer; permit the wrongdoers under the statute to retain all the profits and investment earnings of the business which the wrongdoers admittedly unlawfully obtained, while permitting the wrongdoers to charge off as fees for services the wrongdoers had rendered for themselves. Such a decision could not be expected by the petitioners in the light of the prior decisions rendered in the case, as the opinions of Mr. Chief Justice Gibson, Justices Traynor and Carter make clear in their dissents (App. A, pp. 277-281, 281-306). The concurring opinion of Mr. Justice Schauer (App. A, pp. 274-277), which made the majority decision possible, also indicates the unexpectedness of the result, for concurrence is premised on the promise of the wrongdoer that he will pay $1,018,598.07 to the subscribers of Exchange, although the only legally enforceable judgment entered against the

wrongdoer as a result of the majority decision is one in the sum of $323,300.39.

Petitioners were thus in the position of appellees, on appeal by respondents from an adverse ruling to respondents, which petitioners had no reason to expect, in view of the settled principles of law in the case, would be in any substantial sense disturbed.

Upon the rendition of the opinion and judgment of the Supreme Court, petitioners timely petitioned for rehearing in the said court. It was there stated that the

> "effect of the decision of this Court is to take the lawful property of Exchange and its subscribers and to hand it to Company arbitrarily and capriciously, without basis in law or in fact. The result of this action by the State through its judicial arm is to deprive Exchange and the subscribers of their property without due process of law in violation of the due process clause of the Fourteenth Amendment to the Constitution of the United States" (p. 2).

The petitioners also claimed that

> "the decision and judgment of this Court denies to Exchange and its subscribers the equal protection of the laws in violation of the equal protection clause of the Fourteenth Amendment to the Constitution of the United States" (p. 5),

with appropriate argument and citations of this Court in support of the aforesaid constitutional claims (pp. 2-9).

The petition for rehearing was denied, Mr. Chief Justice Gibson, Justice Traynor and Justice Carter being of the opinion that the petition should be granted.

Reasons for Granting the Writ.

1. The judgment below arbitrarily deprives petitioners of their property, rights and interest without due process of law. The case here is another "glaring instance of the taking of one man's property and giving it to another." (*Thompson v. Consolidated Gas Utilities Corp.*, 300 U. S. 55, 79.) The property of Exchange and its subscribers was arbitrarily handed over to Company in a manner contrary to fundamental principles of justice and against settled usages existing in both the common law of England and the United States. The rulings of the court below were so grossly mistaken as to be impossible in a rational administration of distributive justice.

This Court has held that

> "a State may not by any of its agencies, disregard the prohibitions of the Fourteenth Amendment. Its judicial authorities may keep within the letter of the statute prescribing forms of procedure in the courts and give the parties the fullest opportunity to be heard, and yet it might be that its final action would be inconsistent with that amendment. In determining what is due process of law regard must be had to substance, not to form." (*Chicago, Burlington and Quincy R. R. Co. v. Chicago,* 166 U. S. 226, 234.)

Accordingly, it has been held that a state may not arbitrarily deprive a portion of the members of a solvent association of existing contract rights for the benefit of other members. (*Treigle v. Acme Homestead Association,* 297 U. S. 189, 198.) Nor may a state authorize an individual to take property from another without compensation—it amounts to deprivation of property without due

process of law. (*Chicago, Milwaukee and St. Paul R. R. Co. v. Wisconsin,* 238 U. S. 491, 499.)

> ". . ., it is certain that these words [" due process of law"] imply a conformity with natural and inherent principles of justice, and forbid that one man's property, or right to property, shall be taken for the benefit of another, or for the benefit of the State, without compensation; . . ." (*Holden v. Hardy,* 169 U. S. 366, 390; see also, *Buchanan v. Warley,* 245 U. S. 60, 74.)

So it has been held that the right of the owner ordinarily to fix a price at which his property shall be sold or used is an inherent attribute of the property itself, and, as such, within the protection of the due process of law clauses of the Fifth and Fourteenth Amendments. (*Tyson and Brother v. Banton,* 273 U. S. 418, 429.)

It is thus a well established principle that the arbitrary and capricious taking by a state of the private property of persons or associations, without the owner's consent, for the private use and benefit of another, is not due process, and is a violation of the Fourteenth Amendment of the United States Constitution. (*Missouri Pacific Railway v. Nebraska,* 164 U. S. 403, 417.) It is this violation of constitutional right by the state, among other things, of which petitioners complain.

2. We detail now the legal nature and character of petitioners' property, and the arbitrary manner in which the judgment of the court below operated to deprive petitioners of their property.

(a) A reciprocal insurance exchange is an unincorporated business organization in which the participants, called subscribers, are both insurers and insureds. For

their mutual protection, the subscribers exchange insurance contracts, through the medium of an attorney-in-fact. The subscribers furnish by their premium deposits, the means required for losses and costs, reserves and surpluses of the reciprocal insurance of them all, and therefore are entitled to the equity in the assets of the reciprocal. The position of the attorney-in-fact of a reciprocal exchange is fiduciary in character (App. B, pp. 522-523).

Thus, a reciprocal exchange may be defined as a co-operative enterprise, where the subscribers are not only entitled to the protection afforded by the policies and required to pay the premiums stipulated therein; but they also own the insurance business just as stockholders own their corporation. The subscribers are the owners of their insurance exchange, and as such are entitled to reap the profits accruing from the operation of their insurance business, just as they are required to pay their pro-rata part of the losses and expenses incurred at the exchange. For these reasons, the property of a reciprocal and the equitable and legal property rights of its members are within the guarantees of the Federal Constitution as regards the inhibition against deprivation of property without due process of law and denial of the equal protection of the laws. (See, *Hoopeston Canning Co. v. Cullen,* 318 U. S. 313; *Huber v. Martin* (1906), 127 Wis. 412, 105 N. W. 1031; *Wilson v. Marshall* (Tex., 1949), 218 S. W. 2d 345; *In re Manufacturing Lumbermen's Underwriters* (D. C. W. D. Mo., 1936), 18 Fed. Supp. 114; Notes, *Reciprocal or Interinsurance,* 94 A. L. R. 836; 141 A. L. R. 765; 145 A. L. R. 1121.)

Here, the subscribers of Exchange clearly owned or had a beneficial interest in all the assets of the reciprocal,

in all of its earnings, and in all of the profits obtained from the operation of the business of the reciprocal. On the basis of law and the most fundamental principles of justice, the property, rights and interests of the subscribers could not arbitrarily be turned over by the State to private persons, even with just compensation, and certainly not without it.

(b) In assessing the arbitrary character of the judgment below, it is important to note at the outset some of the facts which are undisputed in the case. It is undisputed that Attorney, the fiduciary of Exchange and petitioners, had substantially the same stock ownership as Company (App. A, p. 260). It is also undisputed that the transfer of the assets of Exchange by Attorney to Company was in violation of express statutory provisions (Cal. Ins. Code, Secs. 1101, 1106) and the principles governing the relation of fiduciary and *cestui que trust* (App. A, p. 260). There is no dispute that Company illegally obtained the business and assets of Exchange, and there is no dispute that Exchange and petitioners are entitled to the return of the aforesaid business and assets so wrongfully obtained, or the value thereof (App. A., pp. 260-261).

In the light of these undisputed facts, it should be noted at the outset that the wrongdoer has never denied that the parties did stipulate a price for the assets of Exchange, to wit, the sum of $1,018,539.07, and has affirmed a moral obligation to pay the said sum (App. A, p. 275). Yet, the judgment of the court below directs restitution to Exchange and its subscribers in the sum of only $323,300.39 (App. A, p. 266). Clearly, this *prima facie* showing of a deprivation of property by

the State warrants initially the close scrutiny of this Court with respect to the claims of denial of federal rights here asserted.

In this connection, too, it should be noted that the dissenting justices below were incisive in their discussion of the legal and factual issues here involved. Mr. Justice Carter described the conclusions reached by the majority as shocking both to his "sense of justice" and his "legal concepts" (App. A, p. 281). The Justice classified the case in his own mind with other "crimes in ink" (App. A, p. 282). Chief Justice Gibson thought that "the majority of the court fails to apply the law correctly to undisputed facts concerning a transaction in violation of statute and, as a consequence, upholds an unjust result" (App. A, p. 277).

Petitioners stress the language of the dissenting justices below because it also demonstrates, in part, that the judgment here was not bottomed upon merely an erroneous application of the law, but was essentially arbitrary and capricious. This is demonstrated fully in the rulings made by the court below with respect to the specific assets and business of Exchange and its subscribers.

(c) The court below has held that Exchange and its subscribers are not entitled to the net profits obtained by Company as a direct consequence of illegally taking over the business of Exchange. This sum was estimated at approximately $4,000,000, or in excess thereof. This ruling was made despite the initial decision of the District Court of Appeal that Exchange had been illegally sold as a going business with its clientele (App. B, p. 528), the denial of hearing by the Supreme Court and

the reaffirmation of this holding by the District Court of Appeal on the second appeal (App. C, p. 251). The ruling was made by the court below despite its agreement that the transfer of the business of Exchange to Company was in violation of the law (App. A, p. 260), and despite the undisputed evidence that the business of Company had increased over 20 million dollars in gross premiums because of the illegal takeover of Exchange (App. A, p. 293). Company, who had acted in violation of State law, was permitted to retain all the net profits directly traceable to the former clientele of Exchange.

On what basis were the subscribers of Exchange, and Exchange, thus deprived of property belonging to them, and to which they would ordinarily be entitled as against a conceded violator of the law who had unlawfully appropriated and used their assets to obtain profits for himself? The essential holding of the court below, based on the "findings," was simply this: Since there was no assurance that any client of Exchange in any year would place his business with Exchange in any succeeding year, it followed that Company could retain all the profits it made from the illegal transfer of the business of Exchange to Company. Thus, Company, after illegally putting Exchange out of business, and thus inviting and virtually compelling the clientele of Exchange to place their business with Company (App. A, p. 299), was permitted by the State to retain the profits of its own wrongdoing—and this upon the assertion that if Company had not obtained the business of Exchange in express violation of law, Exchange could not be sure that it would have had the continued business of its clientele. That Exchange had been a prosperous going concern for many years prior to its illegal transfer is

only one answer to this arbitrary ruling (App. A, p. 299); that *in fact Company did obtain the clientele of Exchange after the illegal transfer,* and did profit from this illegal transfer of the business of Exchange to Company, is another decisive answer.

Thus, the fiduciary who had in violation of the laws betrayed his trust, was permitted to retain the fruits belonging to his *cestui*—because the *cestui* allegedly might not have obtained the same fruits if the fiduciary had not violated his trust. Even if this holding did not disregard the facts plainly revealed in the record, it is clearly arbitrary as a matter of law. The decision runs counter to common law usages and principles of justice inherent in an ordered society.

It is a rule of universal application embedded deep in the common law of England as well as the United States, that no one having the duties of a fiduciary shall be allowed to enter into or profit from a transaction in which he has a personal interest conflicting with the interests of those whom he is bound to protect. (Vinter, *Treatise on the History and Law of Fiduciary Relationship and Resulting Trusts* (Cambridge, 1955), 3rd Ed., p. 145.) Thus, this Court has stated: "The rule of equity is, in every code of jurisprudence with which we are acquainted, that a purchase by a trustee or agent of the particular property of which he has the sale, or in which he represents another, whether he has an interest in it or not,—*per interpositam personam,*—carries fraud on the face of it." (*Michoud v. Girod,* 4 How. (U. S.) 502, 553.) The trustee is at all times disabled from making a profit for himself out of any dealings in the trust property without the express consent of the *cestui*

que trust. (*Chicago, M. & St. P. Ry. Co. v. Des Moines Union Ry. Co.,* 254 U. S. 196, 220.) And no injury sustained by the *cestui que trust* can "upon the general principles of equity, be suffered to pass without a remedy." (*Koehler v. Black River Falls Iron Co.,* 2 Black (U. S.) 715, 721.) All profitable arrangements by wrongdoing fiduciaries "will be condemned whenever properly brought before the courts for consideration." (*Wardell v. Railroad Co.,* 103 U. S. 651, 658.) Hence, "on established principles of equity, and on the plainest principles of justice, the guilty trustee cannot take advantage of his own wrong." (*Westinghouse Electric and Mfg. Co. v. Wagner Electric and Mfg. Co.,* 225 U. S. 604, 620.) "No principle of law is better settled" than that any arrangement by which the fiduciary obtains profits lawfully belonging to his *cestui* will be voidable at the instance of the *cestui.* (*McGourkey v. Toledo and Ohio Cent. Ry. Co.,* 146 U. S. 536, 565.) To permit a fiduciary who has violated his duties to profit from his wrongs would affect the public economy and society adversely. "Were we to sustain it, we should sanction a great moral and legal wrong, give encouragement to faithlessness to trusts, and confidence reposed, and countenance combinations to wrest by the forms of law from the uninformed and confiding their just rights." (*Jackson v. Ludeling,* 88 U. S. 616, 632.)

Moreover, it has been the rule from time immemorial that the malefactor who has wrongfully used the assets of his *cestui* to obtain profits cannot retain such profits on the theory that if the wrong had not been committed, the *cestui* himself would not have made such gains. If the rights of property are to be protected from arbitrary deprivations, restitution cannot be measured by the injury

to the *cestui,* but by the gain obtained by the wrongdoer from the unlawful use of property entrusted to him. Thus, where a director of a bank made a loan of funds in the sum of $30,000 which was in excess of the statutory limits, he could not reduce his liability solely to the amount exceeding that which he could have lawfully made. "To mitigate in his favor the damages resulting from a breach of his statutory duty by resorting to the hypothesis that if he had not disregarded the law in this respect he would have pursued a different course of action within the law, would be an unwarranted resort to fiction in aid of a wrongdoer, and at the expense of the party injured." (*Corsicana National Bank v. Johnson,* 251 U. S. 68, 87-88.) "It makes no difference that the estate was not a loser in the transaction or that the commission was no more than the services are reasonably worth. It is the relation of the trustee to the estate which prevents his dealing in such way as to make a personal profit for himself." (*Magruder v. Drury,* 235 U. S. 106, 120.) ". . . the prohibition is not merely against injuring the estate—it is against profiting out of the position of trust." (*Mosser v. Darrow,* 341 U. S. 267, 273.)

The universality of these rules has been repeatedly attested. (Restatement, *Restitution,* 160(d), 202(c); *Agency,* 403. 404, 407; *Trusts,* 202, 203, 205. See, *Citizen's National Bank v. Appleton,* 216 U. S. 196, 202.)

Thus, both in fact and in law, the judgment of the court below operated to deprive petitioners of their lawful property. This result was reached by an arbitrary disregard of the undisputed facts in the record, and by a complete disregard of fundamental legal principles essential to

the administration of justice and the protection of innocent owners of property against acts of spoilation by unfaithful trustees.

(d) The investment earnings of Exchange amounted at the time of the illegal take-over to $592,322.31, subsequently increased to $711,621.68 (App. A, p. 301). There is no dispute that prior to the illegal transfer of Exchange on December 31, 1948, this so-called Special Surplus Fund was an asset of Exchange (App. A, p. 301). As a result of the illegal transfer by Attorney to Company, the investment earnings of Exchange passed into the hands of Company. Thereafter, the courts declared the transfer illegal and ordered restitution of the business and assets to Exchange. Yet, the court below has permitted this substantial asset, investment earnings, to remain in the hands of the admitted wrongdoer and declared that neither Exchange nor its subscribers may recover such earnings.

The essential basis for this ruling is this: Under the Underwriters Agreement which Attorney had with each of the subscribers, it was provided that the investment income should be set aside as a joint fund to be used for the benefit of Exchange. It was also provided that in the event of discontinuance of the business, any balance, after full provision for liabilities, should be paid to Attorney to defray the expense of, and as compensation for, liquidation (App. A, p. 270). In the opinion of the court below, since Exchange had been discontinued and liquidated, the investment earnings belonged to Attorney, to do with it what it will—not to Exchange. Thus, on the one hand Attorney was condemned for illegally transferring the assets of Exchange; on the

other hand, the illegal conduct was used as a basis for permitting Attorney and Company to keep the assets of the defrauded *cestuis*.

How arbitrary and grossly mistaken this ruling was can be judged from the following considerations:

First, if the transfer of Exchange was not a sale of a going business, but a liquidation within the contemplation of the Underwriters Agreement, then Section 1101 of the Insurance Code did not apply (App. B, p. 528), and the transfer of Exchange would not have been illegal, but a lawful transaction. Yet the majority opinion, including the decisive opinion of the concurring justice, is premised on the view that the transfer was unlawful.

Secondly, if the transfer and assumption agreement of December 31, 1948 was lawful as not within the provision of Section 1101, then the stipulated price of $1,018,539.07 was the minimal sum due the subscribers. Yet the court ordered only restitution in the sum of $323,300.39.

Thirdly, the undisputed evidence showed that the transfer was a sale of a going business and not for purposes of liquidation. In fact, Exchange was never liquidated but carried on as a going business. In fact, the investment earnings was one of the items which Company set up as an asset of Exchange for which Company agreed to pay the subscribers of Exchange over one million dollars (App. A, p. 301). In fact, the Transfer and Assumption Agreement was phrased as one of sale (App. B, p. 528). Government bonds were listed in the agreement as an asset of Exchange in the sum of over three million dollars, without any adjustment or duty

to account for their liquidation (App. B, p. 528). Moreover, "by taking over all assets, assuming all liabilities, including all outstanding policies of the Exchange and becoming directly liable thereon to the policyholders, the Company acquired the whole business of the Exchange as a going concern and would therefore benefit by the increase of its clientele" (App. B, p. 529). Company, therefore, on the undisputed facts, was not acting as a liquidator.

Fourthly, the District Court of Appeal had specifically decided on the first appeal that Exchange had been sold as a going business and not for purposes of liquidation; respondents did not petition for a hearing; the issue was distinctly raised by an intervening subscriber on petition for hearing which was denied by the court below; the same holding was reaffirmed by the District Court of Appeal on the second appeal. Yet this established rule in the case was disregarded by the Supreme Court, not because of some intervening circumstances or change in policy, but by mere fiat. The facts and the law of the case were arbitrarily disregarded and petitioners deprived of an asset clearly belonging to them.

(e) For services rendered by Attorney to Exchange, Attorney was entitled to receive stipulated fees as compensation (App. A, p. 268). On December 31, 1948, Attorney unlawfully transferred the assets of Exchange to Company. *Thereafter,* Company agreed to perform Attorney's obligations and was assigned the right to receive Attorney's fees (App. A, p. 269). Following the unlawful transfer, Company collected from the former clients of Exchange (now allegedly its own clients) the sum of $78,419.13 as fees on dividends and the sum of $246,331.94 as fees on premiums (App. A, p. 303).

These Attorney fees were ordered deducted by the court below from the sums due to the petitioners herein (App. A, p. 268).

The arbitrary nature of this ruling appears plainly from the record. In the first place, the court below has denied all restitution of profits to the subscribers of Exchange because assumedly all the clients of Company after December 31, 1948 were its own, and not those of Exchange. Yet the subscribers of Exchange are required to pay Company the sum of $324,751.07 for the services rendered by Company to its own clients.

In the second place, after December 31, 1948, Company was not acting under the Underwriters Agreement, nor did it purport to do so (App. C, p. 260). Company at all times after December 31, 1948 acted on its own behalf, and it clearly could not charge the defrauded *cestuis* for services it had rendered on its own account and for its own interest.

On consideration of the undisputed record and the established principles of law applicable to the case herein, it is submitted that the judgment below operated arbitrarily, capriciously, and unlawfully to deprive petitioners of their property, rights and interests without due process of law in violation of the Fourteenth Amendment.

3. Moreover, for all of the aforesaid reasons, the decision and judgment of the court below denied to Exchange and its subscribers the petitioners here, the equal protection of the laws in violation of the equal protection clause of the Fourteenth Amendment. The petitioners were arbitrarily and discriminatorily singled out for special treatment wholly unrelated to any public purpose which the State had a right to pursue. The State arbitrarily stripped petitioners of their property, rights and

privileges, creating a single class in the community who could not obtain restoration of the business and assets wrongfully obtained by an unfaithful trustee, acting in violation of the State's own laws.

The denial of the equal protection of the laws was evidenced in three distinct ways. In the first place, by arbitrarily and unlawfully taking the property of Exchange and its subscribers, and giving the said property to Company, an unlawful discrimination *per se* took place. The equal protection of the laws which, by the Fourteenth Amendment, no State can deny to the individual, forbids action by any arm of the State, by which the property of one individual is, without compensation, wrested from him for the benefit of another. (*Reagan v. Farmers Loan and Trust Co.*, 154 U. S. 362, 399.)

In the second place, Section 1101 of the California Insurance Code was enacted for the protection of persons situated as petitioners are here; petitioners were clearly not in *pari delicto* as *cestuis,* with their wrongdoing trustees. Yet all other persons in the same position as petitioners are permitted by the State to retrieve their property so wrongfully obtained. (*Carter v. Seaboard Finance Co.*, 33 Cal. 2d 564, 203 P. 2d 758; *Gatti v. Highland Park Builders, 27* Cal. 2d 687, 166 P. 2d 265; *Poultry Producers, etc. v. Barlow,* 189 Cal. 278, 208 Pac. 93; *Savings Bank of San Diego County v. Burns,* 104 Cal. 473, 38 Pac. 102; *Norwood v. Judd,* 93 Cal. App. 2d 276, 209 P. 2d 24; *Robertson v. Hyde,* 58 Cal. App. 2d 667, 137 P. 2d 703; *Cain v. Burns,* 131 Cal. App. 2d 439, 280 P. 2d 888.) Thus, petitioners were arbitrarily classified as a group by the State who were not entitled to the rights of property which all other similar groups in the State enjoy.

Thirdly, with respect to the fundamental principles affecting the liabilities of fiduciaries and their duty to restore all the property and profits obtained by them in violation of their trust, the court below arbitrarily refused to apply the settled law of the State (App. A, pp. 298-300).

For all of the aforesaid reasons, the judgment below operates to deny petitioners the equal protection of the laws guaranteed by the Fourteenth Amendment. (See *Yick Wo v. Hopkins,* 118 U. S. 356, 373; *Truax v. Raich,* 239 U. S. 33, 43; *Shelley v. Kraemer,* 334 U. S. 1, 14-18.)

4. It is in the light of all of the aforesaid that the jurisdiction of this Court to review is invoked. That judicial action is action of the State is, of course, well established. (*Brinkerhoff Faris Trust & Savings Company v. Hill,* 281 U. S. 673, 680; *Shelley v. Kraemer,* 334 U. S. 1, 14-18.) It was the judicial arm of the State here which on its own motion declared the transfer of the business and assets of Exchange to be in violation of statute; and it was the judicial arm alone that determined the nature, extent and value of the business and assets of the association, denying to the subscribers all restitution of profits, investment earnings and other assets of the illegally transferred reciprocal insurance exchange. That the claim of an arbitrary deprivation of property without due process of law and the denial of the equal protection of the laws by the State in violation of the Fourteenth Amendment is within the review jurisdiction of this Court has been repeatedly affirmed by the Court.

The federal questions here presented are substantial and of public importance. They were specially set up and claimed

in the court below and brought to the attention of the court with fair precision. These questions were created by the unexpected decision of the court, giving the petitioners no prior opportunity to anticipate or assert the said questions. The decision of the court was a surprise and could not have been reasonably anticipated.

In this connection, it should again be noted that on the first appeal, the District Court of Appeal had specifically held that the transfer of Exchange was a sale of the going business and assets, and not a liquidation; that the subscribers were entitled to full restitution of their property and to value of the going business so illegally transferred (App. B); that respondents filed no petition for hearing; that the issues were raised before the Supreme Court by an intervening party, and hearing denied; that the District Court of Appeal on the second appeal reaffirmed the law of the case and specifically held that Exchange and subscribers were therefore entitled to the return of their investment earnings, attorney-in-fact fees and profits directly traceable to the former clients of Exchange (App. C).

In California, a decision of an intermediate appellate court establishes the law of the case after the decision becomes final. In fact, a decision of an intermediate appellate court is the decision of the court of last resort, when no request is made for a review in a higher court. Such a decision is not only binding on the intermediate appellate court when the case is again brought before it, but it is also binding on the supreme court if the case is subsequently appealed to that court.[8]

---

[8]4 Cal. Jur. 2d, Appeal and Error, Section 691, p. 598; *Gore v. Bingaman*, 20 Cal. 2d 118, 120, 124 P. 2d 17; *Deacon v. Bryans*, 212 Cal. 87, 89, 298 Pac. 30; *United D. dging Co. v. Industrial Accident Comm.*, 208 Cal. 705, 712, 294 P c. 922; *Stock v. Meek*, 114 Cal. App. 2d 584, 586, 250 P. 2d 622; *Weichman v. Vetri*, 113 Cal. App. 2d 717, 719, 248 P. 2d 783; *Hill v. Maryland Cas. Co.*, 28 Cal. App. 422, 426, 152 Pac. 953.

When petitioners appeared before the court below as respondents, they had no reason to anticipate that the established law in the case would be abandoned without reason, and that so arbitrary and capricious a ruling would be made as to substantially deprive petitioners of their property, rights and interests in Exchange. The petition for rehearing was therefore the first and only chance to present the federal questions to the court, the questions being created as they were by the unexpected decision of that court. In a variety of situations similar to the one herein, this Court has held that the federal questions are timely raised and will support the exercise of this Court's jurisdiction. (*Missouri v. Gehner,* 281 U. S. 313, 320; *Brinkerhoff-Faris Trust and Savings Co. v. Hill,* 281 U. S. 673, 677; *Saunders v. Shaw,* 244 U. S. 317, 320.)

The majority opinion of the court below purports to rest its decision principally on the "findings" of the trial court. These so-called findings were held by the District Court of Appeal, on appeal, to be merely erroneous conclusions of law or immaterial findings of fact which glossed over the undisputed evidence (App. C). There was simply no evidence in the record to support the conclusion that Exchange had transferred for liquidation purposes, and the undisputed documentary evidence, and the law of the case, established that the business and assets of Exchange had been sold illegally as a going business. Thus, the conclusion that the subscribers of Exchange were not entitled to restitution of profits and the investment earnings of Exchange were baseless in law and fact, and the denial of federal rights clearly established. The evidence clearly showed—and there was none to the contrary, that Company serviced the former clients of Exchange for its own account; yet it was concluded that Company could charge off these services in making restitution for its wrongdoing.

This Court has uniformly held that it will review a state court's findings "where a Federal right has been denied as the result of a finding shown by the record to be without evidence to support it; or where a conclusion of law as to a federal right and a finding of fact are so intermingled as to make it necessary, in order to pass upon the federal question, to analyze the facts." (*Fiske v. Kansas,* 274 U. S. 380, 385-386.) Where federal constitutional rights are asserted, this Court reviews independently both the legal issues and those factual matters with which they are commingled. (*Oyama v. California,* 332 U. S. 633, 636; *Hoover & Allison Co. v. Evatt,* 324 U. S. 652, 659; *Norris v. Alabama,* 294 U. S. 587, 590.)

Conclusion.

For the foregoing reasons, this petition for a writ of certiorari should be granted.

Respectfully submitted,

ROBERT W. KENNY,
FRANK B. BELCHER,
Attorney for Petitioners.

BELCHER, KEARNEY & FARGO,
KENNY & MORRIS,
JEROME POLITZER,
MORRIS E. COHN,
HYMAN & HYMAN,
Of Counsel.

APP.

A

or that she had an opportunity to object at a time when the plaintiffs could have amended their complaint or when they could have dismissed and filed anew. She had no right or privilege to waive her objections. Her objections were in the nature of a plea in bar and not in abatement. The trial court properly sustained her demurrer to the second amended complaint without leave to amend.

For the foregoing reasons and for the additional reasons stated in the majority opinion of the District Court of Appeal of the Second District, Division Two (Cal.App.), 302 P.2d 910, I would affirm the judgment.

McComb, J., concurred.

[S. F. No. 19389. In Bank. Oct. 30, 1957.]

INDUSTRIAL INDEMNITY COMPANY (a Corporation) et al., Respondents, v. GOLDEN STATE COMPANY, LTD. (a Corporation), et al., Defendants; G. W. THOMAS DRAYAGE & RIGGING COMPANY, INC. (a Corporation), et al., Defendants and Appellants; THE ROBERT L. JOHNSON CORPORATION (a Corporation), Intervener and Appellant.

[On hearing after decision by the District Court of Appeal, First Appellate District, Division Two, Civ. No. 16940 (144 A.C.A. 244, 301 P.2d 112) reversing with directions judgment of the superior court. Judgments affirmed.]

[1] **Insurance—Reciprocal Insurers—Transfers.**—In an action for declaratory relief regarding the rights of nonconsenting subscribers of a reciprocal insurance exchange under an agreement transferring its business to plaintiff indemnity company, profits arising from the placement of policies by former subscribers of the exchange with the company were not part of the business or assets of the exchange, and it was not unfair and inequitable to allow the company to keep the claimed profits, where expert witnesses showed that, in evaluating the business and assets of an established business insurance business, future profits or prospective earnings are not taken into account, and where other witnesses testified that the transfer agreement had

---

[1] See Cal.Jur.2d, Insurance, § 99 et seq.

McK. Dig. References: [1-3] Insurance, § 10.5; [4] Damages, § 34; [5] Parties, § 25.

no influence on their decisions to place business with the company, that they knew the company and exchange had had the same management and when the exchange went out of business they placed their business with the company for that reason, but they also stated that they would not have done so if they could have obtained a better "deal" elsewhere, and that some business was placed with the company at the client's request because of ownership interest in the company.

[2] **Id.—Reciprocal Insurance Transfers.**—In an action for declaratory relief regarding the rights of nonconsenting subscribers of a reciprocal insurance exchange under an agreement transferring its business to plaintiff indemnity company, findings that a partnership acting as attorney for the exchange was entitled to receive a percentage of premiums for its services as attorney-in-fact, that the subscribers had no right to these fees, that the company agreed to perform the obligations for the attorney and was assigned the right to receive the unpaid attorney fees, and that these fees constituted no part of the business or assets of the exchange, were supported by evidence of an underwriters agreement under which the attorney-in-fact had full power to reinsure and to enforce rights and discharge liabilities in the same way as an individual subscriber could do, by the transfer agreement which provided that the company would reinsure all outstanding policies and perform all obligations of the exchange under the terms of the policies, each of which incorporated the underwriters' agreement, and by a document executed between the attorney and the company whereby the company assumed the obligations of the attorney and the attorney assigned its rights to the management fees.

[3] **Id.—Reciprocal Insurers—Transfers.**—In an action for declaratory relief regarding the rights of nonconsenting subscribers of a reciprocal insurance exchange under an agreement transferring its business to plaintiff indemnity company, the trial court did not err in holding that a special surplus fund was not a part of the business or assets of the exchange, where it appeared from an underwriters' agreement that a partnership acting as attorney for the exchange was entitled to the fund "if Exchange discontinues business" as compensation for winding up the affairs and liquidation and that the exchange had been discontinued; and a further finding that this fund was assigned to the company as compensation for work performed in connection with the liquidation of the exchange, less the portion required to reimburse the attorney for future costs of liquidation, and that the subscribers had no right or claim to this surplus since it was not a part of the exchange's business or assets, was proper and did not result in the company being unjustly or unfairly enriched, where the benefits it thereby received did not arise as a consequence of the transfer agreement, but as a result of the attorney's determination not to issue any new policies.

[4] **Damages—Interest.**—In an equitable proceeding, the matter of awarding or withholding interest is within the sound discretion of the court, and interest should be awarded only when such an award is fair and equitable under the facts of the case; in an action for declaratory relief regarding the rights of nonconsenting subscribers of a reciprocal insurance exchange under an agreement transferring its business to plaintiff indemnity company, the court did not abuse its discretion in refusing to allow interest on an award to defendants where it found that the company had not acted in bad faith.

[5] **Parties—Intervention—Status of Intervener.**—In a stockholders' derivative action interveners are but volunteers in the main original cause, and their counsel may not participate in the presentation of the main case save as counsel for the main stockholders may consent or the court may permit; the court is not bound to permit the intervention of others of the same class if their interests are properly protected.

APPEAL from a judgment of the Superior Court of the City and County of San Francisco. Albert C. Wollenberg, Judge. Affirmed.

Action for declaratory relief regarding the rights of nonconsenting subscribers of a reciprocal insurance exchange under an agreement transferring its business to plaintiff indemnity company, in which a cross-complaint for restitution was filed. Judgment ordering restitution to defendants for amount less than that sought, affirmed.

Belcher, Kearney & Fargo, Frank B. Belcher, Kenny & Morris, Robert W. Kenny, Jerome Politzer, Morris E. Cohn and Hyman & Hyman for Defendants and Appellants.

Thelen, Marrin, Johnson & Bridges and Edward J. Ruff for Respondents.

McCOMB, J.—Industrial Indemnity Exchange (hereinafter referred to as Exchange) was a reciprocal insurance organization handling workmen's compensation insurance. Industrial Indemnity Company (hereinafter referred to as Company) also handled workmen's compensation insurance. There was considerable interrelation between Exchange and Company but no competition. Industrial Underwriters (hereinafter referred to as Attorney) was the managing entity of Exchange and Company.

In a reciprocal exchange the participants, called under-

writers or subscribers, exchange insurance contracts for their mutual protection through the medium of an attorney-in-fact, who also sets rates, settles losses, compromises claims and cancels contracts. Attorney acted in this capacity for Exchange under an agreement known as Underwriters Agreement. In return for its services it received a percentage of the premiums deposited by the subscribers and was required to furnish offices and personnel for Exchange's operations out of this percentage.

Attorney, a partnership with substantially the same stock ownership as Company, also furnished offices and personnel for the latter. The Insurance Commissioner objected to the interlacing by Attorney of its private corporation (Company) and Exchange. He made certain recommendations looking to the separation of the management of these entities or the elimination of possible conflicting loyalties through a combination of their activities.

An agreement was entered into between Company and Exchange whereby the insurance policies of Exchange would be transferred to and reinsured by Company as of December 31, 1948. The agreement provided that Company would service and run out all policies then in force and would pay the subscribers of Exchange an amount equal to the value of the entire net worth of Exchange as determined by such run-out. Consents were obtained from 98 per cent of the subscribers of Exchange to this agreement.

Subsequently Company brought an action for declaratory relief regarding the rights of the nonconsenting subscribers. Cross-complaints were filed by several sets of these subscribers. After trial, judgment was rendered in favor of Company, and the cross-complaints were ordered dismissed.

Two separate sets of defendants appeal, (1) G. W. Thomas Drayage and Rigging Company, Inc., W. R. Ballinger and Son, a corporation, and Minna M. Ballinger (hereinafter referred to as defendant Thomas Drayage and Rigging Company), and (2) Robert L. Johnson Corporation, for itself and as representative of all similarly situated cowner subscribers of Exchange (hereinafter referred to as defendant Johnson Corporation).

On appeal it was held that the contract between Company and Exchange was illegal and void in violation of section 1101 of the Insurance Code. (*Industrial Indem. Co.* v. *Golden State Co.*, 117 Cal.App.2d 519 [256 P.2d 677].) The appellate court (1) reversed the judgment in favor of Company and remanded the case to the trial court with directions to deny

all declaratory relief to plaintiffs, and (2) stated that "in the cross-actions, relief will be granted [to appellants] only with respect to the consequences of the illegality of the transfer and assumption agreement. . . . ." (See p. 540.) It then directed the trial court to grant defendants "such relief as the court will deem fit to enable them to recover in their representative capacity for subscribers the *business and assets obtained by Company in consequence of the agreement herein held to be invalid*. . . ." (See pp. 540-541.) (Italics added.)

After the reversal of the trial court's judgment defendant Johnson Corporation filed a petition for judgment and decree pursuant to its interpretation of the effect of the appellate court's remittitur. Defendant Thomas Drayage and Rigging Company moved to strike this petition upon the ground that Johnson Corporation was a mere "intervenor" and as such not entitled to act on terms of equality with the other defendants. This motion was granted by the trial judge. Thereafter judgment was entered in favor of the defendants in the sum of $323,300.39. From this judgment both defendant Thomas Drayage and Rigging Company and defendant Johnson Corporation appeal.

APPEAL OF DEFENDANT THOMAS DRAYAGE AND RIGGING COMPANY

In view of the former decision on appeal the trial court was limited to a determination of this issue: *What business and assets were obtained by Company in consequence of the "Transfer and Assumption Agreement"?*

There can be no question that the "agreement" held to be invalid referred to the Transfer and Assumption Agreement that was the basis of the litigation. An examination of the record discloses that the following findings of fact are sustained by substantial evidence:

"IV. Coincident with the issuance to Underwriters of the Certificate of Authority to act in liquidation of the Exchange, and on November 4, 1953, Company transferred to Underwriters and Underwriters accepted on behalf of Exchange and its subscribers, and with the approval of the Advisory Committee of Exchange, all of the business, property and assets of Exchange remaining in its hands after satisfaction of liabilities of the Exchange and which had been received by Company in consequence of the Transfer and Assumption Agreement. Underwriters has thereafter at all times continued in possession of and presently holds such business, property and assets for distribution to the subscribers of the

Exchange in liquidation of its business and affairs. *As of March 31, 1954, the net worth, representing the excess of assets over liabilities, including reserve for losses incurred and to be incurred, of the business, property and assets so transferred, exclusive of the Special Surplus Account, was $323,300.39.* (Italics added.)

"V. The business, property and assets of Exchange received by Company in consequence of the Transfer and Assumption Agreement and thereafter transferred to Underwriters as found herein, included all assets and liabilities of Exchange as reflected on the balance sheet of December 31, 1948, and which thereafter arose or accrued and all policies of insurance in force on the books of the Exchange as of December 31, 1948, and the entire experience thereon including the development of claims and premiums. All of the business, property and assets of Exchange of every kind or character received by Company from Exchange at any time, and all value attributable thereto have been returned by Company to Underwriters and are included within the net worth as set forth in Paragraph IV of these Findings. The business, property and assets of Exchange do not include any policies written by the Company after December 31, 1948, for or on behalf of any former subscribers of Exchange and the net worth as set forth in Paragraph IV of the findings does not reflect any value with regard to such policies and no accounting of any profits made by Company on such policies is any part of these findings.

"VI. Under the provisions of the Transfer and Assumption Agreement, Company, with regard to policies of insurance in force in the Exchange as of December 31, 1948, took over for its own account that portion of the 1948 policy year occurring after December 31, 1948, and under the provisions of the Transfer and Assumption Agreement no adjustment was to be made to the net worth of the Exchange payable to the subscribers with regard to this portion of the experience on those policies. That portion of the 1948 policy year taken over by Company for its own account developed to be unprofitable. This loss amounted to $156,600.53. All policies of insurance in force with Exchange as of December 31, 1948 and the entire experience on those policies, including the experience on the entire 1948 policy year, and the entire experience on policies previously issued by Exchange and expired on December 31, 1948, are a part of the business and assets of the Exchange and because of the invalidity of the Transfer and Assumption Agreement are for the account of

the Exchange. This entire experience on policies of insurance in force with Exchange as of December 31, 1948, as well as the entire experience on policies previously issued by Exchange and expired on December 31, 1948, is reflected in the amount of net worth as set forth in Paragraph IV of these Findings.

"VII. All policies of insurance at any time issued by the Exchange, including those in force as of December 31, 1948, were issued subject and pursuant to the terms and provisions of an Underwriters' Agreement executed by each of the subscribers. Under the terms of such Underwriters' Agreement, a true copy of which has been received in evidence as Defendants' Exhibit No. 6, Underwriters was appointed as Attorney-in-Fact and was entitled to receive as its fee 25 per cent of all compensation premium deposits received and 5 per cent of all savings credited to each subscriber. The subscribers or any of them did not at any time have any right to any portion of these fees to be paid to Underwriters and such fees were at all times the property of Underwriters or its assignee. The Underwriters' Agreements have at all times been in full force and effect with regard to all policies of insurance issued by or on behalf of Exchange.

"VIII. By written agreement dated January 2, 1949, a true copy of which has been received in evidence as Plaintiffs' Exhibit No. 3, following the execution of the Transfer and Assumption Agreement, Company agreed to perform for Underwriters after January 1, 1949, all of Underwriters' obligations relating to policies of insurance at any time issued by Exchange and Underwriters transferred to Company its rights to receive fees under the Underwriters' Agreement and as yet unpaid. Company performed all services required by it to be performed under such agreement. Following the decision of the District Court of Appeal, Company and Underwriters without notice to the defendants and cross-complainants G. W. Thomas Drayage & Rigging Company, Inc., W. R. Ballinger & Son, a corporation, and Minna M. Ballinger, terminated and cancelled the agreement of January 2, 1949, and without notice to the defendants and cross-complainants G. W. Thomas Drayage & Rigging Company, Inc., W. R. Ballinger & Son, a corporation, and Minna M. Ballinger, executed a written agreement dated November 15, 1953, a true copy of which has been received in evidence as Plaintiffs' Exhibit No. 4, acknowledging payment to Company of fees payable to Underwriters under said Underwriters Agreements and releasing Company of all claims by Underwriters to any

fees theretofore collected by Company. All of such Attorney-in-Fact's fees have been properly taken into account in computing the net worth referred to in Paragraph IV of these findings and the subscribers have no right to any portion of such fees paid to or received, directly or indirectly, by Company or Underwriters and they do not constitute any part of the business, property or assets of Exchange to which the subscribers are entitled.

"XIII. All policies of insurance in force on the books of Exchange as of December 31, 1948, were placed with Exchange by insurance agents or brokers who were free to place this business with such insurance carriers as they chose. The decision as to the placement of any policy of workmen's compensation insurance by an insurance agent or broker was made each year as a new and distinct item of business taking into consideration all elements of coverage, cost, management and other relevant matters. The placement of a policy of insurance by an insurance agent or broker with Exchange in any one year did not mean that it would be placed with Exchange in a succeeding year.

"XIV. All policies of insurance placed with Company after December 31, 1948, on behalf of persons, firms or corporations who had formerly been policyholders of Exchange were voluntarily placed with Company as new items of business by insurance agents or brokers who were free to place such policies with such insurance carrier as they chose. The decision as to the placement of such policies of workmen's compensation insurance is made each year by the insurance agent or broker as a new item of business, taking into consideration all elements of coverage, cost, management and other relevant matters. The placement of a policy of insurance with Company in any one year does not mean that it will be placed with Company in any succeeding year. In view of these circumstances surrounding the placement of business, it cannot be determined and there is no evidence that any of these policies will be placed with the Company in the future. *None of these policies was placed with Company by reason of or as a consequence of activities of Company being performed under, or arising as a consequence of, the Transfer and Assumption Agreement or because Company was regarded in any sense as being the successor of Exchange.* All policies placed with Company were so placed because the coverage, cost and service afforded by management of Company was attractive to the policyholder and insurance agent or broker. (Italics added.)

"XVIII. Company did not use, succeed to or receive for its own account new or different information concerning past or prospective policyholders or succeed to or receive any new or different management, name, insignia, goodwill or agency plant from Exchange as a consequence of the Transfer and Assumption Agreement, nor did it at any time or in any manner receive any management, name, insignia, goodwill or agency plant which was a part of the business, property or assets of or belonged to the subscribers of Exchange.

"XXI. In connection with its business of insurance management, Underwriters out of its own funds employed and paid all personnel, bought and owned all equipment and developed and paid its own agency plant. None of this personnel, equipment, or agency plant was or at any time has been the property of the Exchange or the subscribers of the Exchange or any part of the business, property or assets of the Exchange.

"XXII. No policies of insurance are any part of the business, property or assets of Exchange except those policies of insurance which had been placed with and were in force on the books of Exchange and no value is to be given to nor allowance made for any prospective business not in force on the books of Exchange on December 31, 1948, in determining the business, property or assets of Exchange.

"XXVI. It is not true that the compensation paid or to be paid to or for the account of Attorney-in-Fact under the provisions of the Underwriters' Agreements is in any amount or for any period any part of the business, property or assets of the Exchange or the subscribers to the Exchange.

"XXX. It is not true that any policies of insurance written or to be written by Industrial Indemnity Company on or after January 1, 1949, or at any time for, with, or on behalf of persons, firms or corporations who were former subscribers of the Exchange or any other persons, firms or corporations, or the profits therefrom or net earnings or any earnings thereon are or were any part of the business, property or assets of the Exchange or the subscribers of the Exchange or are any part of the business, property or assets of Exchange obtained by Company in consequence of the Transfer and Assumption Agreement.

"XXXI. It is not true that there are any other assets not yet discovered or identified which constitute business, property or assets of the Exchange or which were the business, property or assets of Exchange on December 31, 1948, or at any other time and which are not reflected in the net worth as

referred to in Paragraph IV of these findings, and it is true that all of the business, property and assets of the Exchange and all of the business, property and assets of Exchange received by Company in consequence of the Transfer and Assumption Agreement are now in the possession of the Exchange, subject to the control of the Advisory Committee of the Exchange, Underwriters and the Insurance Commissioner of the State of California and are reflected in the net worth as set forth in Paragraph IV of these findings."

It logically follows that since the trial court's findings are supported by evidence and covered the issues the appellate court had ordered retried, the judgment in the principal amount should be affirmed.

Defendant Thomas Drayage and Rigging Company urges the following contentions, which are without merit:

[1] *First*: That the profits arising from the placement of policies by former Exchange subscribers with Company were part of the business or assets of Exchange.

The trial court found that none of the profits arising from the placement of policies by former Exchange subscribers with Company was part of the business or assets of Exchange. (See Findings IV, V, XIII, XIV, XXII and XXX, *supra*.)

Defendant does not attack these findings on the ground of insufficiency of the evidence, but on the ground that it is unfair and inequitable to allow Company to keep the claimed profits. This contention is unsound. The testimony of two expert witnesses showed that in evaluating the business and assets of an established insurance business, future profits or prospective earnings are never taken into account. In other words, there is no value placed upon the possibility of future earnings.

The reason is succinctly stated by one witness, Mr. Best, as follows: "Now, in the writing of that type of business [workmen's compensation] there is never any right of a policyholder to demand that his policy be renewed, there is never any right on the part of the company to demand that that policyholder renew his policy with that company. The business, in fact, is controlled first of all by the policyholder himself. He decides where he wants to put it. Then he hires a broker or agent to look after it, and he has a considerable say as to just where that business is to go, that is to what carrier company or reciprocal or what have you. Then finally the company gets the business. It happens that in that particular field there is a tremendous shifting from company to company as these annual policies expire. I had occasion to observe that particular

matter, which is very striking. There is great competition for those big policies, and company A may have it this year and company B gets it next year and company C gets it the third year and so forth, so it is a transitory sort of business, and not only that, but actually in such a business every year's operation—for that matter every renewal of a policy or acceptance of a new policy—is a new venture, so to speak. It has nothing to do with what went on before. That being so, and it being well understood that whoever carries the risk is entitled to the premium and to any profit that results because he carries the risk and must bear the loss, if there is a loss, it has always been considered that only the business that is on the books at a particular moment when the valuation is to be made can be given any weight whatever; future business itself is too uncertain."

Likewise, the testimony of witnesses Rainey, Wright, Hullin, Lynch, Williams and Miller, all of whom are brokers of workmen's compensation insurance, support the questioned findings. They testified that policies are reviewed annually, about two months before the expiration date, loss experience is checked, the current market is also checked for risk-loss ratio, premium brackets, dividends, etc.; that they try to "make the best deal they can" for their clients; that the practice and custom of the "American Agency system" is that the brokers "own" the business, i.e., their customer list; and that only the broker and carrier know the expiration dates. Being the "owner," the broker is free to place the business where he wishes on expiration. Each witness testified that he had placed business with Company, had placed it previously with Exchange, and had also placed business with other companies. They also stated that the Transfer and Assumption Agreement whereby Company took over Exchange had no influence whatever on their decisions to place with Company.

Several witnesses testified that they knew Company and Exchange had had the same management and when Exchange went out of business they placed their business with Company for that reason, but they also stated that they would not have done so if they could have obtained a better "deal" elsewhere. There was also testimony that some business was placed with Company at the client's request because of ownership interest in Company. Defendant stipulated that seven other named brokers would testify similarly.

Defendant made no attempt to rebut the foregoing testimony and produced no witnesses who testified to the contrary. Defendant's argument appears to be that even though future

profits are not and were not an asset of Exchange, Company should not be allowed to keep them, not because there is any evidence of bad faith, breach of fiduciary duty, mishandling of funds, or fraud, but because the District Court of Appeal originally found the Transfer Agreement to be void. It is obvious that there is no merit in this argument.

[2] *Second*: That Company is not entitled to the "Attorney-in-Fact fees."

The questioned fees were derived from the unearned premiums of the 1948 policies, which were all written prior to the Transfer and Assumption Agreement. The trial court found that Attorney was entitled to receive a percentage of premiums for its services as attorney-in-fact; that the subscribers at no time had any right to these fees; that Company agreed to perform the obligations for Attorney and was assigned the right to receive the Attorney Fees as yet unpaid; and that these fees constituted no part of the business or assets of Exchange. (See Finding VIII, *supra.*) The trial court also found that it was not true that the compensation paid for the account of Attorney was any part of the business or assets of Exchange. (See Finding XXVI, *supra.*)

The evidence supporting the foregoing findings is: (a) the Underwriters Agreement; (b) the Transfer and Assumption Agreement; and (c) the agreement whereby Company assumed the obligations of Attorney and Attorney assigned its rights to the management fees.

The trial court was correct in finding that the Underwriters Agreement remained in effect and covered all policies written in 1948. The Transfer and Assumption Agreement did not expressly or impliedly supersede the Underwriters Agreement. Under the Underwriters Agreement the Attorney-in-Fact had full power to reinsure; it also had full power to enforce rights and discharge liabilities in the same way as an individual subscriber could do.

The Transfer and Assumption Agreement provided that Company would reinsure all outstanding policies and would perform all the obligations of Exchange under the terms of the policies. The Underwriters Agreement was a part of each policy written.

The application of insurance with Exchange provided: "This application if granted is subject to the foregoing statements and declarations and is further subject to the conditions of the following agreement which are made a part hereof and which are agreed to by the applicant as follows:

. . .'' Thereafter follows the Underwriters Agreement. The last clause of the agreement provides: ''This agreement is strictly limited to the use and purposes herein expressed and no other purpose; it may be terminated at any time by the subscriber or the Attorney by either giving to the other 10 days' written notice, but, until such termination shall remain in full force and effect as to all policies of insurance hereafter issued and accepted by the subscriber; within a reasonable time after such termination the subscriber's account shall be liquidated and any funds standing to his credit returned.''

The Transfer and Assumption Agreement did not purport to terminate the Underwriters Agreement or to terminate the outstanding policies. It provided for (1) reinsurance of outstanding policies, (2) the transfer of assets of Exchange, (3) assumption of liabilities of Exchange in payment to the subscribers of the ''adjusted net worth'' of Exchange, (4) time and amount of payments to subscribers, (5) payment directly to subscribers (1948 policyholders), (6) the keeping by Company of all accounts, and (7) a waiver by Attorney of all rights to the Special Surplus Fund of Exchange, reading as follows: ''In consideration of the covenants and agreements of the other parties hereto as herein contained, the Attorney-in-Fact hereby waives any and all rights it may have in and to the special surplus of the Exchange, and will not at any time hereafter assert any rights whatever in or to said special surplus.''

That the parties to the Transfer Agreement did not intend it to supplant the Underwriters Agreement is evidenced by the document executed between Attorney and Company on January 2, 1949, whereby Company agreed to perform and discharge all the obligations of Attorney with respect to the insurance issued by Exchange, and Attorney assigned to Company its rights thereunder and agreed that it would not ''at any time make any claim whatever that it is entitled to the whole or any portion of the account designated as 'Special Surplus' as shown on the books of the Exchange as of the close of business on December 31, 1948.''

There is no contention that the services were not performed in accordance with the agreement or that Attorney did not have a right to assign these fees. It thus appears from the Underwriters Agreement that the Attorney Fees were never a part of the assets of Exchange, even though they may have been obtained by Company as a consequence of the Transfer and Assumption Agreement.

[3] *Third*: That the trial court erred in holding that the

Special Surplus Fund was not a part of the business or assets of Exchange.

The Underwriters Agreement provided: "A Special Surplus Fund shall be created to which shall be set aside all investment income; it shall be a joint fund and no part thereof shall be credited to the account of any individual subscriber; it shall be used for the benefit of the Exchange as the Advisory Committee and Attorney may agree; if the Exchange discontinues business, any balance, after full provision for liabilities to the satisfaction of the Insurance Commissioner, shall be paid to the attorney to defray the expense of, and as compensation for, liquidation."

In accordance with the foregoing provision, the trial court found that the Special Surplus Fund was, under the Underwriters Agreement, to be reserved for expenses incurred in connection with liquidation and payable to Attorney; that on November 15, 1953, this was assigned to Company as compensation for work heretofore performed in connection with the liquidation of Exchange, less such portion as required to reimburse Attorney for future costs of liquidation; and that the subscribers have no right or claim to this surplus since it was not a part of Exchange's business or assets. (Finding IX.*)

After the District Court of Appeal's first decision, Attorney and Company entered into an agreement restoring the business and assets of Exchange to Attorney as Attorney-in-Fact of Exchange, subject to Attorney's obtaining a certificate of authority from the Insurance Commissioner. Thereafter such a certificate was issued for the limited purpose of dis-

*Finding IX reads: "Under the terms of the Underwriters' Agreements, Exchange at all times maintained a Special Surplus Fund consisting of all investment income received on Exchange funds; this fund, in the event Exchange discontinues business and after full provision for liabilities to the satisfaction of the Insurance Commissioner, is to be paid to Underwriters to defray the expenses of and as compensation for liquidation. The amount of this fund as of March 31, 1954, was $592,322.31. Underwriters by written agreement dated November 15, 1953, a true copy of which has been received in evidence as Plaintiffs' Exhibit No. 38, has agreed without notice to the defendants and cross-complainants G. W. Thomas Drayage & Rigging Company, Inc., W. R. Ballinger & Son, a corporation, and Minna M. Ballinger, to pay to Company as compensation for work heretofore performed by Company on behalf of Underwriters in connection with the liquidation of the Exchange, a sum equal to the special surplus which Underwriters may receive, less such portion of the special surplus as may be required to reimburse Underwriters for incurred and future costs of liquidation. The subscribers of Exchange have no right or claim to any portion of this special surplus and it does not constitute any part of the business, property or assets of the Exchange to which the subscribers are entitled."

charging the obligations under the policies and Underwriters Agreement, winding up the affairs of Exchange, and carrying out the liquidation of the assets, business and affairs of Exchange.

The Transfer and Assumption Agreement provided, in paragraph VII: "In consideration of the covenants and agreements of the other parties hereto as herein contained, the Attorney-in-Fact hereby waives any and all rights which it may have in and to the special surplus of the Exchange, and will not at any time hereafter assert any rights whatever in or to said special surplus."

The agreement of January 2, 1949, between Attorney and Company, paragraph (3), provided: "The Attorney-in-Fact further agrees that it will not at any time make any claim whatever that it is entitled to the whole or any portion of the account designated as 'Special Surplus' as shown on the books of the Exchange as of the close of business on December 31, 1948."

Defendant argues that Company waived its rights to this fund. The trial court found otherwise. After the first decision of the District Court of Appeal, Company reasserted its right to the fund in its answer to defendant's petition for retrial.

Under the Underwriters Agreement, Attorney-in-Fact was entitled to this fund "if Exchange discontinues business," as compensation for winding up the affairs and liquidation. The question then arises whether Exchange has been "discontinued." The trial court found that it had, and the evidence supports the finding.

It is to be noted that the Insurance Commissioner issued the certificate of authority only to the extent necessary to wind up the affairs of Exchange. Exchange has no authority to issue new policies. Since the sum is not a part of the assets of Exchange, it is clear that the trial court's disposition of it was correct.

It is also to be noted that defendant does not claim the policy contract, which included the Underwriters Agreement, was unfair or that the policyholders (subscribers of Exchange) had been taken advantage of by Company. The 1948 policyholders were in no sense injured nor was Company unfairly enriched at their expense.

Defendant's arguments to the contrary are unsupported by the record. The court found, and the evidence amply supports the finding, that future profits, Attorney Fees and the Special Surplus Fund were not items obtained by Company as a con-

sequence of the illegal Transfer and Assumption Agreement. The trial court also made the following findings:

"XI. All policies of insurance at any time issued to subscribers of Exchange were for a term period of one year, and the relationship of the subscriber to the Exchange terminated upon the expiration of any such policy, except for incompleted matters as to such policy, unless continued by the issuance of a new and further policy. Underwriters had no obligation to issue any new or further policy for any subscriber of the Exchange upon the expiration of an existing policy, and a subscriber had no right to demand that any such policy be issued. Underwriters, under the terms of the Underwriters' Agreements and the policies of insurance issued to subscribers, had the power to cancel any such policies of insurance and to terminate the Underwriters' Agreements at any time upon ten days' notice and in the event of such termination, Underwriters had the duty to liquidate the subscribers' account and return any funds standing to the subscribers' credit. The Underwriters' Agreements contained no provision whereby the Attorney-in-Fact could be replaced by the subscribers.

"XII. Prior to December 31, 1948, Underwriters with the knowledge and approval of the Advisory Committee of the Exchange determined that it would not thereafter issue any new policies of insurance in the Exchange and no such policies have been issued. All policies of insurance issued to subscribers of Exchange expired by their terms on or before December 31, 1949. Since December 31, 1948, Exchange has been engaged in no business except for the liquidation of Exchange."

The foregoing findings, which are not disputed, show that defendant and the other 1948 policyholders have not been injured by the execution of the Transfer and Assumption Agreement, and that they have received all to which they were entitled. Therefore, they have not suffered either injury or damage.

However, defendant claims that Company should be deprived of the benefits it received as a result of the discontinuance of business by Exchange. This claim is based upon the contention that Company has been unjustly or unfairly enriched. The evidence does not support this conclusion. During 1948 and several years prior thereto Exchange wrote the largest volume of premiums of all reciprocal workmen's compensation insurance carriers in California. When Attorney determined to discontinue business, as it had a right to do, other insurance carriers, including Company, would, of course,

obtain a share of this business. This additional business would accrue to Company regardless of the Transfer and Assumption Agreement so long as it was competitive with other carriers.

The record discloses that no policy, except where there was ownership interest involved, would have been placed with Company unless its rates or service were as good or better than other carriers. In short, the profits derived from this additional business did not arise as a consequence of the Transfer and Assumption Agreement, but as a result of Attorney's determination not to issue any new policies.

The prior decision of the District Court of Appeal held that none of the workmen's compensation business acquired by Company prior to 1948 was a consequence of the interlocking relationship between Attorney and Company, as "the Company did not at any time in the operation of its business use any funds, facilities or information belonging to, or secured through, the Exchange." (See 117 Cal.App.2d 519, 537 [256 P.2d 677].)

On retrial, the court found that "Company did not use, succeed to or receive for its own account new or different information concerning past or prospective policyholders or succeed to or receive any new or different management, name, insignia, goodwill or agency plant from Exchange as a consequence of the Transfer and Assumption Agreement, nor did it at any time or in any manner receive any management, name, insignia, goodwill or agency plant which was a part of the business, property or assets of or belonged to the subscribers of Exchange." (Finding XVIII, *supra*.)

Company received nothing, either prior to or as a consequence of the illegal Transfer and Assumption Agreement, that would give it an advantage over any other carrier in the field. It likewise appears from the record that under the "American Agency system," as practiced and in use in the workmen's compensation field, the renewals or expirations (customer lists) are owned by the agent or broker, and not by the insurance carrier. It is thus evident that Company has not been unjustly or unfairly enriched.

[4] Finally, defendant claims the trial court erred in not allowing interest on the award. The trial court's position was correct. This was an equitable proceeding, and the rule is settled that in such a proceeding the matter of awarding or withholding interest is within the sound discretion of the trial court. Interest is awarded only when such an award is fair and equitable in consideration of the facts of the particular case. (See *Leonard* v. *Huston*, 122 Cal.App.2d 541,

548 [3] [265 P.2d 566]; *Board of County Commrs.* v. *United States*, 308 U.S. 343, 352 [60 S.Ct. 285, 84 L.Ed. 313]; *Stockton Theatres, Inc.* v. *Palermo*, 121 Cal.App.2d 616, 632 [264 P.2d 74]; see also 90 C.J.S. (1955), Trusts, § 338, p. 584, and cases cited in nn. 60 and 61.)

In the present case the trial court found that Company had not acted in bad faith, and therefore we cannot say it abused its discretion in refusing to allow interest on the award.

APPEAL OF DEFENDANT JOHNSON CORPORATION

[5] Defendant Johnson Corporation contends that its cross-complaint was improperly dismissed from the action. This contention is not sound. In a stockholders' derivative action interveners are but volunteers in the main original cause, and their counsel may not participate in the presentation of the main case save as counsel for the main stockholders may consent or the court may permit. (*Mann* v. *Superior Court*, 53 Cal.App.2d 272, 280 [2] [127 P.2d 970] [hearing denied by the Supreme Court].)

In the present case the trial court was not bound to permit the intervention of others of the same class if their interests were properly protected. So far as the record discloses here, defendant Johnson Corporation's interests were fully and properly protected, and therefore the trial court did not err in dismissing its cross-complaint.

In view of our conclusions it is unnecessary to discuss other questions argued by counsel.

The judgment and orders are each affirmed.

Shenk, J., Schauer, J., and Spence, J., concurred.

SCHAUER, J.—I concur. It is my view that the issues of law have been, as such, adequately discussed and correctly disposed of in the opinion prepared by Mr. Justice McComb. Nevertheless, because opinion diverges sharply among some of the justices, it appears proper to briefly supplement our discussion.

In the arguments for the dissenting theory, respondents have been termed "wrongdoers." That term is ordinarily connotive of evil intent as well as illegal act. Under any permissible view of the record the term seems to me to be an unduly harsh epithet to be applied. As appears from the opinion of the District Court of Appeal on the first appeal in this case (*Industrial Indem. Co.* v. *Golden State Co.* (1953), 117 Cal.App.2d 519, 527 [256 P.2d 677]), the issue of illegality of the Transfer and Assumption Agreement by reason

of the then provisions of section 1101 of the Insurance Code was injected into the case by that court. Until then respondents were willing and fully intended to carry out their obligations under that agreement, which would have meant that the subscribers would have received $1,018,589.07, rather than only the $323,300.39 awarded them by the judgment which is now being affirmed. Despite this situation, the president of Company, who is also one of the partners of Attorney, testified that, regardless of the outcome of the case, it was the intention of respondents to pay the subscribers an amount equivalent to that which the subscribers would have received under the Transfer and Assumption Agreement, less costs of litigation. I believe that this further demonstrates the good faith of respondents, already conclusively shown,[1] and

[1]It is to be remembered that it is established that the Transfer and Assumption Agreement was entered into in good faith and had the approval of the insurance commissioner. Obviously, in the conduct of respondents, there was no union of act and evil intent. The opinion of the District Court of Appeal on the first appeal (*Industrial Indem. Co.* v. *Golden State Co.* (1953), *supra*, 117 Cal.App.2d 519) carefully notes many significant facts. Pertinent to the discussion, the opinion reads:

"[P. 526] The court found in nearly all respects for plaintiffs and against the cross-complainants . . . The judgment declared in substance that past subscribers had no interest in the Exchange and were not entitled to participate in any distribution; that the transfer and assumption agreement was fair and equitable, validly executed and binding on all past and present subscribers of Exchange, and that they had no right to any net worth or assets of Exchange except as provided in said agreement, that said agreement distributed to the subscribers all they were entitled to in the most equitable, reasonable and practical manner and that subscribers had no interest in the business or assets of Company. . . .

"[P. 527] We have concluded that the original action for declaratory relief should have been denied because the agreement to which it relates is void as violating section 1101 of the Insurance Code, expressly made applicable to reciprocal exchanges by section 1282 of said code. Section 1101 reads insofar as applicable to this case: 'An admitted insurer's officers, directors, trustees and any persons who have authority in the management of the insurer's funds, shall not, unless otherwise provided in this code: . . . (c) Directly or indirectly purchase, or be interested in the purchase of, any of the assets of the insurer.' Section 1106, Insurance Code, reads in part: 'Any person violating . . . Sections 1101, . . . is guilty of a misdemeanor.'

"This exact point was not raised by any of the parties, but was briefed specially at the request of this court. . . .

"[P. 534] In this case the court below made most elaborate findings as to all circumstances on which it based its holding that the cross-defendants have not breached their fiduciary duty. . . .

"[P. 537] As we have held that the establishing of the circumstances under which the Attorney engaged in workmen's compensation insurance business of its own and the weighing of these circumstances in relation to the duty of fairness and good faith incumbent on the Attorney as a fiduciary were matters of fact, the decision of which by the trier of facts is as a rule binding on appeal, it seems evident that the findings stated

evidences their continuing intention to live up to their own obligations as set forth in the agreement, if that will result in payment of a greater sum to the subscribers than would result under the judgment of the court. Respondents' unwillingness to accept the benefits of a windfall judgment—a judgment correct within the law but seemingly unjust in an equitable sense—is conduct which impresses me as more deserving of commendation than censure.

We ordinarily expect law and justice to go hand in hand; the state enacts and enforces law to achieve justice. Nevertheless, that the enforcement of law does not always result justly was recognized many generations ago, when the concept of equity was born. As declared in *Owens* v. *McNally* (1896), 113 Cal. 444, 450 [45 P. 710, 33 L.R.A. 369], "the law failing by reason of its universality, equity, to promote justice, makes good its imperfections. [Citations.]" But, regrettably, imperfections sometimes appear which not even the reach of equity can make good.

The principle articulated in section 1101 of the Insurance Code and relied upon by the District Court of Appeal in holding the Transfer and Assumption Agreement to be illegal and void was manifestly intended to promote justice. Its application in this case seems to me, however, to have resulted in a judgment which, understandably, some may feel on its face achieve the contrary, not so much, perhaps, because of the substance of the judgment now under consideration as because of the inability of the court to enforce an agreement which had been found to be fair and just to all parties but which was held to be technically invalid. The upholding and performing of a fair and just contract would certainly appear to be promotive of justice. But the decision, on the first appeal in this case, that such contract could not be sustained has long since become final and cannot now be disturbed. That

---

are fatal to the appeal with respect to the claims of subscribers of Exchange to the business of Company unless appellants have shown that they are not supported by the evidence. This they have failed to do. . . .

"[P. 539] Under these circumstances it is not for us to say that the ultimate findings of the court below are necessarily improper inferences nor can we hold as a matter of law, contrary to said findings, that the Attorney breached its fiduciary duty to subscribers when it engaged in the writing of workmen's compensation insurance through the medium of Company or that the business of Company was in equity the property of Exchange. We are the more satisfied that this result is not unjust because the gain by Exchange of all profits of the business of Company without participation in them by any of Company's insureds would have given the subscribers of the Exchange a windfall wholly out of line with the setup of such Exchange."

decision, in the light of the findings of fact at the first trial, which were held to be supported by the evidence, coupled with the findings in this second trial, which are also supported by the evidence, clearly precludes, under existing law, any relief beyond that granted. Similar applications of the principle (nonenforceability of a fair contract because of statutory illegality) resulting in unjust enrichment of a party have repeatedly divided this court. (See *Loving & Evans*, v. *Blick* (1949), 33 Cal.2d 603, 615, 617 [204 P.2d 23]; *Franklin* v. *Nat C. Goldstone Agency* (1949), 33 Cal.2d 628, 633 [204 P.2d 37]; *Fraenkel* v. *Trescony* (1957), *48 Cal.2d 378, 383, 388 [309 P.2d 819].) In this connection it may be noted that under a 1955 amendment to the Insurance Code it appears that such an agreement as that which gave rise to the current controversy may now be legally made and performed, thus indicating that no basic principle of public policy, fairness, or justice was violated when it was executed in 1948. Neither that fact, however, nor even the overruling of the cited cases, could now affect the finality of the decision on the first appeal. I believe that the judgment of the trial court now being affirmed recognizes and correctly applies the law to the facts, which is all that the court under the limitations of the earlier holding could do, and that the carrying out by respondents of their legally unenforceable but nevertheless voluntarily self-recognized and now self-declared obligations under the Transfer and Assumption Agreement, brings this unfortunate litigation to the most desirable conclusion which under existing circumstances can be attained.

Shenk, J., concurred.

GIBSON, C. J.—I dissent. In my opinion, the majority of the court fails to apply the law correctly to undisputed facts concerning a transaction in violation of statute and, as a consequence, upholds an unjust result.

The law of the case, as decided on the prior appeal (*Industrial Indem. Co.* v. *Golden State Co.*, 117 Cal.App.2d 519 [256 P.2d 677]), is that the Transfer and Assumption Agreement by which Company took over the whole business of Exchange was void because it violated section 1101 of the Insurance Code[1] and that the subscribers are entitled to recover the business and assets obtained by Company as a consequence

*Advance Report Citation: 48 A.C. 376, 381, 386.

[1]Section 1101 of the Insurance Code provides: "An admitted insurer's officers, directors, trustees and any persons who have authority in the

of that agreement. The code section was designed to protect persons such as the subscribers against the detrimental action of those in a position like that of Attorney. The subscribers, therefore, are not to be considered *in pari delicto* with Attorney and Company (*Carter* v. *Seaboard Finance Co.*, 33 Cal.2d 564, 574 [203 P.2d 758]; see *Lewis & Queen* v. *N. M. Ball Sons*, *48 Cal.2d 141, 152 [308 P.2d 713]), and the latter are the parties legally responsible for the violation, even if they acted in good faith.

It is undisputed, and the trial court found, that the Transfer and Assumption Agreement was considered fair and equitable by Attorney and Company, that it was concluded openly with the consent of the Insurance Commissioner and of 98 per cent of the subscribers, and that the net worth of Exchange which would have been distributed to subscribers in accordance with the agreement, had it not been invalid, would have amounted to $1,018,589.07. Nevertheless, the judgment of the trial court affirmed by the majority awards the subscribers no more than $323,300.39 as the value of the business and assets of Exchange taken over by Company. Thus, as the decision of the majority stands, those for whose protection the violated statute was enacted will receive less than one-third of what would have been theirs under the agreement, whereas those who are responsible for the violation will not only retain all of the benefits of the agreement but also obtain a large financial windfall. It is true that the president of Company, who is also one of the partners of Attorney, testified that, regardless of the outcome of the case, it was the intention of Company to pay the subscribers an amount equivalent to that which the subscribers would have received under the void agreement, minus costs of litigation, but a court cannot be justified in rendering a decision which compels a litigant to rely on the magnanimity of his opponent to obtain equity, unless such a result is unavoidable. I am satisfied that a proper application of the law to the facts before us not only permits but requires a more equitable result.

There are three matters in controversy, namely, the profits realized by Company from the issuance of new insurance policies to former subscribers of Exchange, the sum referred to as attorney-in-fact fees, and the amount constituting the special surplus fund. Although I share the view of the ma-

---

management of the insurer's funds, shall not, unless otherwise provided in this code: . . . (c) Directly or indirectly purchase, or be interested in the purchase of, any of the assets of the insurer."

*Advance Report Citation: 48 A.C. 139, 151.

jority that there is sufficient evidence to support the trial court's finding that the business profits were not obtained as a consequence of the void Transfer and Assumption Agreement, I cannot agree as to the disposition of the other two items. The facts relating to them are undisputed, and only questions of law are presented. The conclusion of the majority, in my opinion, results from an erroneous application of the Underwriters Agreement to the illegal transaction under consideration.

There can be no doubt that, under the Underwriters Agreement, any right of Attorney to attorney-in-fact fees must arise from performance of the managerial functions connected with the business of Exchange. Undeniably, Attorney did not perform such functions between January 1, 1949, when the Transfer and Assumption Agreement was to take effect, and November 6, 1953, when assets of Exchange were restored by Company.[2] It is obvious, therefore, that Attorney would not be entitled to fees allocable to that period.

Nor can Company have any right to attorney-in-fact fees. Under the Underwriters Agreement, the fees were, of course, intended as compensation for management services rendered to Exchange, and, admittedly, Company did not at any time perform such services for Exchange but, instead, performed them solely for its own account, mistakenly believing that it was the owner of Exchange's business. Any claim by Company to the contractual amount of fees would necessarily depend upon an effective assignment of Attorney's rights, and there was no such assignment. The purported assignment in January of 1949 was, by its terms, made because of the Transfer and Assumption Agreement.[3] It was merely one step in the overall transaction by which Company illegally took over the business of Exchange, and, therefore, it was as invalid as the main agreement. (*Stockton Morris etc. Co.* v. *California etc. Corp.*, 112 Cal.App.2d 684, 689-690 [247 P.2d 90].) The agreement

[2]The agreement for restoration of assets was executed on November 3, 1953, but it was conditioned upon the Insurance Commissioner's issuance to Attorney of a Certificate of Authority, and such a certificate was issued on November 6, 1953.

[3]The purported assignment in 1949, after reciting that Attorney was the Attorney-in-Fact for Exchange and was entitled to fees for the performance of certain services, provided:

"WHEREAS: effective 12:01 A.M., January 1, 1949, all of the assets of the EXCHANGE were transferred to COMPANY and COMPANY assumed all of the obligations of the EXCHANGE including the obligation to perform certain services, for which performance the ATTORNEY-IN-FACT was, in turn, obligated to the EXCHANGE; and

"WHEREAS, under its agreement with the EXCHANGE, the ATTORNEY-IN-FACT would be entitled to receive certain moneys in addition to

of November 15, 1953, in which Attorney released its claim to fees in favor of Company, could not, of course, constitute an effective transfer to Company with respect to the period in question, since, as we have seen, Attorney had no right to fees allocable to that period.

In concluding that, by operation of the Underwriters Agreement, the sum treated as attorney-in-fact fees is not an asset of the subscribers, the majority opinion reasons, "There is no contention that the services were not performed in accordance with the agreement or that Attorney did not have a right to assign these fees." As shown above, however, insofar as the period between January 1, 1949, and November 6, 1953, is concerned, Attorney did not perform any services, Company did not perform any services "in accordance with the agreement," and no effective assignment was made. In my view, it is apparent that, even if, as assumed by the majority opinion, the Underwriters Agreement continued in force, it does not support the position taken but, to the contrary, compels the conclusion that the amount under consideration is an asset of the subscribers.

The erroneous use of the Underwriters Agreement by the majority in holding that the subscribers are not entitled to the special surplus fund is equally apparent. The agreement provided, "A Special Surplus Fund shall be created to which shall be set aside all investment income; . . . it shall be used for the benefit of the Exchange as the Advisory Committee and Attorney may agree; if the Exchange discontinues business, any balance, after full provision for liabilities to the satisfaction of the Insurance Commissioner, shall be paid to the attorney to defray the expense of, and as compensation for, liquidation." Obviously, the fund was to be an asset of Exchange with respect to which Attorney could have no right unless there was a discontinuation and liquidation of the business in keeping with the agreement.

The majority opinion concludes, in effect, that there has been a discontinuation of the type contemplated in the agreement. That conclusion is manifestly unsound. It requires holding that the provision for the benefit of Attorney was intended to refer not only to an ordinary discontinuation of

---

those earned or received by it on or prior to the close of business on December 31, 1948,

"NOW, THEREFORE, IT IS AGREED BY AND BETWEEN THE PARTIES HERETO AS FOLLOWS:"

In ensuing provisions, Company agreed to perform the services required of Attorney, and Attorney transferred and assigned its rights under agreements with Exchange.

business but also to a situation where, as here, through Attorney's participation, the business was discontinued solely because of a sale of assets in violation of a statute which was designed to protect persons such as the subscribers against the detrimental action of those in a position like that of Attorney. Clearly, nothing done by Company during its illegal possession of the business may be regarded as constituting liquidation, since the law of the case, as decided on the prior appeal, is that the void transfer agreement under which Company acted was not an agreement for the liquidation of Exchange but one for Company's purchase of assets and assumption of liabilities. (*Industrial Indem Co.* v. *Golden State Co.*, 117 Cal.App.2d 519, 528 [256 P.2d 677].) While it appears to be true that, because of the unlawful transaction, the business cannot now be revived and must be liquidated, this cannot reasonably be treated as giving rise to any right in Attorney. The special surplus fund, which, on March 31, 1954, amounted to $592,322.31, was, of course, intended to relate to full and regular liquidation. To hold that Attorney is entitled to the fund for liquidating the remnants of a business in whose illegal destruction it participated represents an absurd application of the Underwriters Agreement. In addition, such a holding would ignore the rule that one may not take advantage of his own wrong, since the statutory violation for which Attorney and Company are responsible constitutes a wrong, regardless of good faith.

In view of the position taken by the majority, it is not necessary in this dissent to consider whether, notwithstanding the illegality of the action of Company and Attorney, some allowance should be made in their favor for the actual cost of services performed. It is clear, however, that a proper determination with respect to attorney-in-fact fees and the special surplus fund would substantially increase the recovery of the subscribers. For example, it appears to be undisputed that, even if an allowance for actual costs were made, refusal to grant Company attorney-in-fact fees would alone entitle the subscribers to approximately $324,000 more than the amount awarded in the erroneous judgment affirmed by the majority.

I would reverse the judgment.

Traynor, J., concurred.

CARTER, J.—I dissent.

The reasoning and the conclusion reached by the majority and concurring opinions are shocking to both my sense of jus-

tice and my legal concepts. If I am not mistaken this case will be appropriately classified in the annals of jurisprudence with other "crimes in ink." It is obvious to my mind and I think it should be to any unbiased person that if this court should apply the law of the case to the undisputed factual background as disclosed by the record the inevitable result would be a reversal of the judgment of the trial court with directions to retry the case in accordance with the law of the case as declared in the first decision of this case by the District Court of Appeal rendered on April 30th, 1953 (see *Industrial Indem. Co.* v. *Golden State Co.*, 117 Cal.App.2d 519 [256 P.2d 677]). Simply stated, the undisputed factual situation appears to be: Plaintiff Industrial Indemnity Company, through its officers, and by means of their financial interests, controlled both Industrial Indemnity Exchange (hereinafter referred to as Exchange) and the Industrial Underwriters (hereinafter referred to as Attorney-in-Fact). Prior to January 1st, 1949, Exchange was the largest writer of workmen's compensation insurance in California. It was a reciprocal insurance organization of which defendants Golden State Company, Ltd., G. W. Thomas Draying & Rigging Company, Inc., W. R. Ballinger & Son, Minna M. Ballinger, Johnson Corporation, et al. were subscribers. Exchange was then in competition with plaintiff Industrial Indemnity Company in writing policies of workmen's compensation insurance.

On December 21st, 1948, Industrial Indemnity Company, Industrial Indemnity Exchange, acting through its Attorney-in-Fact and Advisory Committee, and Industrial Underwriters entered into a Transfer and Assumption Agreement which provided in part:

"That in consideration of the mutual covenants herein contained the parties hereto do hereby agree as follows:

"I. REINSURANCE

"A. Effective as of 12:01 A.M., January 1, 1949, Exchange does hereby cede and Company does hereby completely reinsure all policies of insurance issued by the Exchange and in effect as of said time and date.

"B. The Company agrees to carry out and perform all of the obligations of the Exchange under the terms of said policies of insurance or any of them, and to be directly liable thereon to the policyholders of the Exchange. The Company also undertakes to declare and pay policyholders' dividends in respect to policies of insurance issued by the Exchange according to the terms of such policies on the basis of the Exchange dividend policy theretofore in effect.

"II. TRANSFER OF ASSETS

"A. Effective 12:01 A.M., January 1, 1949, *Exchange will sell, assign and transfer and it does hereby sell, assign and transfer to Company all of the assets of the Exchange of whatever nature and kind, whether now known or hereafter discovered, owned by it at said time and date, and whether or not appearing on its books as of said time and date.*

"III. ASSUMPTION OF LIABILITIES AND PAYMENTS TO BE MADE

"A. Company agrees to accept and does hereby accept the assignment and transfer of such assets as of the time and date herein provided, and agrees to perform the acts hereinafter set forth, and to pay the amounts computed as hereinafter provided at the times and in the manner hereinafter more particularly set forth.

"B. In addition to the obligations assumed under paragraph I hereof, Company agrees to assume and discharge and does hereby assume any and all other liabilities of the Exchange of whatever nature or kind in any manner incurred prior to 12:01 A.M., January 1, 1949.

"C. *Amounts to be paid*: As compensation for the assignment and transfer to it of the assets of the Exchange, Company will pay to the persons and in the manner herein set forth an amount equal to the 'adjusted net worth' of the Exchange, computed as follows:

"1. UNADJUSTED NET WORTH:

"An audit of the books of Industrial Indemnity Exchange as of the close of business December 31, 1948, will be caused to be made by the Company and the Advisory Committee as soon after December 31, 1948, as possible, and, in any event, prior to the end of the month of February, 1949. Such audit shall be conducted on the same basis as audits of the Exchange have been made in recent years, except that the reserve for losses and claims shall be computed upon the case basis rather than the 'Schedule P' formula basis. Upon completion of the audit, an audited balance sheet as of December 31, 1948, will be prepared by the Company, and upon approval by the Insurance Commissioner, shall be delivered to each member of the Advisory Committee of the Exchange. For purposes of such financial statement, the assets shall be valued at market value as of December 31, 1948. A copy of such financial statement will thereupon be attached to this agreement, marked 'Exhibit A,' and except for possible errors

in computation and possible omissions all the parties hereto agree to be and are hereby bound by said financial statement.

"The unadjusted net worth of the Exchange as of the close of business on December 31, 1948, shall be the sum of the excess of statutory reserves for losses over case basis reserves for such losses, the reserve for contingencies, special surplus and unassigned surplus as shown on said financial statement. . . .

"IV. TIME AND AMOUNT OF PAYMENTS

"The total net payments, equal to the adjusted net worth, to be made by the Company to the subscribers of the Exchange will be made by the Company at the following times:

"A. $1,000,000.00 on or before March 31, 1949;

"B. $500,000.00 on or before March 31, 1950;

"C. Any balance remaining due, on or before March 31, 1952.

"By mutual agreement between the Company and the Advisory Committee, and conditioned upon the prior approval of the Insurance Commissioner, the dates for and amounts of any of the foregoing payments may be postponed or changed, as may be justified by future developments. . . .

"VII. WAIVER BY ATTORNEY-IN-FACT OF RIGHTS IN SPECIAL SURPLUS:

"In consideration of the covenants and agreements of the other parties hereto as herein contained, the Attorney-in-Fact hereby waives any and all rights which it may have in and to the special surplus of the Exchange, and will not at any time hereafter assert any rights whatever in or to said special surplus. . . .

"IX. RETURN OF SUBSCRIBERS' INDIVIDUAL SURPLUS FUND DEPOSITS:

"The Company agrees to pay to the individual subscribers entitled thereto the total amount of the subscribers' individual surplus fund deposits paid or maintained as of December 31, 1948, by each of said subscribers, such payment to be made to each individual subscriber entitled thereto on or within a reasonable time after the termination of his policy. However, in the event that at such time there shall be due and owing from such subscriber any premium arising under a policy issued by the Exchange on or before December 31, 1948, such subscriber's individual surplus fund deposit shall, to the extent of any such premium due and unpaid, be credited or applied in payment thereof." (Emphasis added.)

At the time this agreement was executed K. K. Bechtel was president of Industrial Indemnity Company. He was also managing partner of Industrial Underwriters, Attorney-in-Fact for Industrial Indemnity Exchange. While Mr. Bechtel did not sign the contract on behalf of Industrial Indemnity Company, he signed it as managing partner of Industrial Underwriters, Attorney-in-Fact for Industrial Indemnity Exchange and as a member of the Advisory Committee of Industrial Indemnity Exchange and as managing partner of Industrial Underwriters. The contract was executed on behalf of Industrial Indemnity Company by Thomas G. McGuire, Executive Vice-President. It was found by the trial court and conceded by all of the parties to this litigation that Mr. Bechtel and his associates in Industrial Indemnity Company, by virtue of their financial interests, controlled all of the parties to said agreement. In this respect the District Court of Appeal in its first decision of this case cited *supra* stated: "Neither is it denied nor could it be denied that the members of the Attorney are persons who have authority in the management of the funds of the Exchange. The interrelation between the Attorney and the Company, which is at the basis of this whole case, leaves no doubt that said partners in the Attorney would be interested in, at least indirectly, any purchase made by the Company. In this respect it will suffice to quote from finding 16 of the court the following passus which is not attacked:

" 'The stock ownership of Industrial Indemnity Company has at all times been substantially the same as the ownership of Industrial Underwriters, a partnership, the attorney-in-fact of the Exchange.' " (117 Cal.App.2d 519, 527, 528 [256 P.2d 677].)

Prior to the execution of said Agreement an attempt had been made by Mr. Bechtel and his associates to procure the consent of all of the subscribers of the Exchange to said Transfer and Assumption Agreement and they succeeded in obtaining the consent of approximately 98 per cent of said subscribers. Industrial Indemnity Company then commenced an action in the superior court of the City and County of San Francisco seeking declaratory relief regarding the rights of subscribers of Industrial Indemnity Exchange, under said Agreement. The nonconsenting subscribers cross-complained in said action, claiming that all the insurance business transacted by Industrial Indemnity Company belonged in equity to Exchange, from whose business it was alleged to have been disloyally diverted by Industrial Underwriters, the Attorney-

in-Fact of said Exchange, whose partners substantially owned the stock of Industrial Indemnity Company.

The trial court awarded plaintiff Industrial Indemnity Company the relief demanded by it in said action and denied any relief to the objecting subscribers.

The subscribers appealed and the District Court of Appeal in its decision cited *supra*, reversed the judgment and decree of the trial court and laid down the following rules which constitute the law of the case and should have controlled the subsequent disposition of the case:

(1) The District Court of Appeal specifically held that the Transfer and Assumption Agreement constituted a sale of all of the assets and business of Exchange to Company. In this respect the court stated at page 530: "Respondents urge, however, that even if it were an actual sale, *as we consider it*, the agreement would come under an exception to section 1101 [of the Insurance Code]. . . ." (Emphasis added.)

(2) The District Court of Appeal specifically held that Exchange was not in liquidation. In response to the contention of Company that the Transfer and Assumption Agreement was actually an agreement to liquidate, the court stated at pages 528 and 529: Company contends that "the transaction was actually an agreement to liquidate. However that is not the case. . . . Another circumstance which shows that the Company did not act merely as liquidator is of greater importance from a practical point of view. By taking over all assets, assuming all liabilities, including all outstanding policies of the Exchange and becoming directly liable thereon to the policyholders, the Company acquired the whole business of the Exchange as a going concern and would therefore benefit by the increase of its clientele."

(3) In answer to Company's contention that the Insurance Commissioner could require the sale of Exchange to Company (section 1105) the District Court of Appeal specifically held at page 530: "The contention is without merit. The Commissioner did not require and had no power to require the sale of the whole business of the Exchange as a going concern. To 'require' in this sense means 'to demand; to claim as by right and authority; to exact.' (Webster.) The Commissioner did not demand it and had no authority to demand it."

(4) The District Court of Appeal held that the Transfer and Assumption Agreement was illegal and void because in contravention of section 1101 of the Insurance Code, which

provides that an admitted insurer's officers, directors, trustees or any persons having authority to manage the insurer's funds shall not "directly or indirectly purchase, or be interested in the purchase of, any of the assets of the insurer." It further held that section 1106 makes any violation of section 1101 a misdemeanor. In this respect the court stated at page 527: "We have concluded that the original action [brought by Company] for declaratory relief should have been denied because the agreement to which it relates is void as violating section 1101 of the Insurance Code, expressly made applicable to reciprocal exchanges by section 1282 of said code."

(5) With respect to the contentions made by Company that it acted in "good faith" because it did not know the law forbade the transaction and made such a violation of the law a crime, the court stated at page 532: "Even if their said conduct was in good faith and proper, as found by the court below, it would create a precedent wholly adverse to the purpose of section 1101, subdivision (c), if they were permitted to solve the difficulties so caused by absorbing the going business of the Exchange into their privately owned corporation, even if the price they paid for it would be adequate."

(6) The District Court of Appeal specifically held that the officers of plaintiff and the other parties to the Agreement were acting in a fiduciary capacity and could not seize for themselves the assets of Exchange as contemplated by the Transfer and Assumption Agreement. At page 533 the court said: "Since the leading case of *Guth* v. *Loft*, 23 Del.Ch. 255 [5 A.2d 503], it has been generally accepted that a corporate officer or director may not seize for himself to the detriment of his company business opportunities in the company's line of activities which the company has an interest and prior claim to obtain, and that if he seizes them in violation of his fiduciary duty the corporation may claim for itself all benefits so obtained by him. The doctrine was applied in this state to joint venturers in *MacIsaac* v. *Pozzo*, 81 Cal.App.2d 278 [183 P.2d 901], and is equally applicable in all situations in which a person manages or transacts business for another or for others to whom he stands in a fiduciary relation without being trustee of an express trust. The position of the attorney-in-fact of a reciprocal insurance exchange, who manages the business of the exchange under powers of attorney of the subscribers, who provide the means for the reciprocal insurance enterprise, is fiduciary in character to the same extent as that of the management of an incorporated mutual insurance company, although neither is a real trustee. (See *Caminetti* v.

State Mut. Life Ins. Co., 52 Cal.App.2d 321, 323 [126 P.2d 165]) and the doctrine of corporate opportunities is equally applicable."

With respect to the language of the court concerning the evidence as supporting the findings of fact of the trial court that Company had not breached its fiduciary duty toward Exchange, it is obvious that it was referring to the contention of Exchange that it was entitled to the *whole business of Company* because it said at page 539: "Under these circumstances it is not for us to say that the ultimate findings of the court below are necessarily improper inferences nor can we hold as a matter of law, contrary to said findings, that the Attorney *breached its fiduciary duty to subscribers when it engaged in the writing of workmen's compensation insurance through the medium of Company or that the business of Company was in equity the property of Exchange. We are the more satisfied that this result is not unjust because the gain by Exchange of all profits of the business of Company without participation in them by any of Company's insureds would have given the subscribers of the Exchange a windfall wholly out of line with the setup of such Exchange.*" (Emphasis added.)

The findings of the trial court that Company had not breached its fiduciary duties toward Exchange were, therefore, held by the District Court of Appeal to relate to Company's participating in the workmen's compensation insurance field before the illegal take-over of Exchange; and to Exchange's contention that it was entitled to *all* of *Company's* business developed prior to such take-over. It is obvious that this discussion on the part of the District Court of Appeal does *not* relate to Company's breach of its fiduciary duty to Exchange in executing the Transfer and Assumption Agreement, which it had theretofore held to be an invalid, illegal and void agreement of purchase and sale.

The conclusions reached in the District Court of Appeal opinion were as follows: 1. "Although we hold that the subscribers of Exchange are not entitled to the business built up by Company in general—and then they are necessarily not entitled either to the business of its wholly owned subsidiary, Industrial Service Company, mentioned separately on appeal—*they have a right to the business taken over by Company in consequence of the transfer and assumption agreement, which we have held to be invalid.* If they so desire they are entitled to have that matter wound up in these equity proceedings and for that purpose the judgment denying all

relief on the cross-complaints [by Exchange] will also have to be reversed." (Emphasis added.)

2. The trial court was directed to "deny all declaratory relief to plaintiffs [Company] on the ground that the agreement as to which it is prayed for is void as contrary to law. . . ."

3. The trial court was directed to grant such relief to Exchange as to permit them to recover in "their representative capacity for subscribers *the business and assets obtained by Company in consequence of the agreement herein held to be invalid.* . . ." (Emphasis added.)

The gist of the decision of the District Court of Appeal cited *supra* which is now the law of the case, may be summarized as follows: The Transfer and Assumption Agreement dated December 21st, 1948, constituted an attempted sale of all of the business and assets of Exchange to Industrial Indemnity Company. Such a sale was illegal in face of the objection of the nonconsenting subscribers to Exchange. The illegality of such sale and transfer was based both upon common law rules and statutory law of this state. It violated common law rules because the officers of the participating companies were acting in a fiduciary capacity to the subscribers of Exchange. Those officers violated their fiduciary duty under the common law by appropriating to their own use the property of the subscribers of Exchange without their consent. The legal effect of this transaction was that the directors and officers of Company, who, because of their financial interests, controlled Exchange, Industrial Underwriters and Attorney-in-Fact, used their power of control to deprive subscribers of Exchange of their property rights in Exchange in violation of their fiduciary duty to subscribers which no court of justice should sanction. The transaction was in violation of the statutory law of this state because expressly and specifically prohibited by section 1101 of the Insurance Code, the violation of which section was made a misdemeanor by section 1106 of the Insurance Code. Because the entire transaction was illegal for the reasons above stated and the participants therein were guilty of a crime under the law of this state, Industrial Indemnity Company had no standing in a court of justice to enforce the Agreement and its action brought for this purpose was ordered dismissed. The court, however, reserved to the nonconsenting subscribers the right to resort to the court for the protection of their rights which should contemplate the restoration by Company to the Exchange of the business and assets illegally appropriated or an award of compensation

adequate to cover the value of such business and assets so illegally appropriated together with all accrued increments therefrom.

It is obvious that the trial court on the retrial of the case utterly disregarded the law of the case as declared by the first opinion of the District Court of Appeal cited *supra*. In direct violation of the law of the case announced in said decision the trial court held and found that Industrial Indemnity Company took over the business and assets of Exchange for the purpose of liquidation and that Exchange was not entitled to the going concern value of its business at the time of the illegal transaction. It charged Exchange with the cost and expenses incurred by Company in winding up the business of Exchange and awarded to Company assets of Exchange worth considerably over a million dollars without awarding subscribers of Exchange any compensation therefor.

The obviously palpable result and legal effect of the decision of the trial court on the retrial of this case was to deprive the subscribers of Exchange of their property which consisted of a valuable beneficial interest in the business of Exchange without due process of law. A clear and concise statement with respect to the protection of the right of private property under the Fourteenth Amendment to the Constitution of the United States was made by Mr. Justice Day of the Supreme Court of the United States in *Buchanan* v. *Warley*, 245 U.S. 60, at page 74 [38 S.Ct. 16, 62 L.Ed. 149]. Speaking for a unanimous court he there declared: "The Federal Constitution and laws passed within its authority are by the express terms of that instrument made the supreme law of the land. The Fourteenth Amendment protects life, liberty, and property from invasion by the States without due process of law. Property is more than the mere thing which a person owns. It is elementary that it includes the right to acquire, use, and dispose of it. The Constitution protects these essential attributes of property. *Holden* v. *Hardy*, 169 U.S. 366, 391 [18 S.Ct. 383, 42 L.Ed. 780]. Property consists of the free use, enjoyment, and disposal of a person's acquisitions without control or diminution save by the law of the land. 1 Blackstone's Commentaries (Cooley's Ed.), 127." In *Brinkerhoff-Faris Co.* v. *Hill*, 281 U.S. 673 [50 S.Ct. 451, 74 L.Ed. 1107], the Supreme Court of the United States specifically held that judicial action as state action is within the due process clause of the Fourteenth Amendment. At pages 681 and 682 the court stated: "But, while it is for the state courts to determine the adjective as well as the substantive law of

the State, they must, in so doing, accord the parties due process of law. *Whether acting through its judiciary or through its legislature,* a State may not deprive a person of all existing remedies for the enforcement of a right, which the State has no power to destroy, unless there is, or was, afforded to him some real opportunity to protect it. Compare *Postal Telegraph Cable Co.* v. *Newport,* 247 U.S. 464, 475-6 [38 S.Ct. 566, 62 L.Ed. 1215]." (Emphasis added.)

We have here a situation where the beneficial interests—the property rights of Exchange and subscribers in the business and assets of Exchange are taken from them by Company without their consent and in violation of both common law rules and statutory law, and Company and its officers committed a crime under the law of this state when it and they appropriated the property of Exchange and subscribers to the use of Company by means of the illegal and void Transfer and Assumption Agreement. Under every concept of law, equity, justice or fair dealing, Exchange and subscribers are entitled to have their property or its full value restored to them with all accrued increments. But under the majority decision in this case, property, admittedly worth approximately two million dollars at the time it was illegally appropriated by Company, with all its accrued increments of many millions of dollars, is retained by Company, and subscribers are awarded the paltry sum of $323,300.07, probably 2 or 3 per cent of the present value of the property and its accrued increments now in the hands of Company. I cannot conceive of such a travesty on justice occurring under any system for the administration of justice entitled to the respect of honest, fair-minded men. I have always believed that the requirement of the due process clauses of both our state and federal Constitutions contemplates a fair and honest application of the settled rules of law to every established factual situation. Only by this process may justice be achieved. The result reached by the majority here today does violence to every concept of due process of law with which I am familiar.

The majority glosses over the damning fact that in seizing the business and assets of Exchange in the manner shown by the record here, Company and its officers committed a crime—a misdemeanor (see Ins. Code, §§ 1101, 1106) — and since overt acts were committed in the furtherance of an unlawful agreement, the crime amounted to a felony under the law of this state (Pen. Code, § 182; *Calhoun* v. *Superior Court,* 46 Cal.2d 18 [291 P.2d 474]; *People* v. *Malotte,* 46 Cal.2d 59 [292 P.2d 517]; *Lorenson* v. *Superior Court,* 35 Cal.2d 49

[216 P.2d 859]; *People* v. *Robinson*, 43 Cal.2d 132 [271 P.2d 865]; *People* v. *Vanderpool*, 20 Cal.2d 746 [128 P.2d 513]).

The illegal and void Transfer and Assumption Agreement itself makes out a clear case of conspiracy to violate sections 1101 and 1106 of the Insurance Code by the participants in this illegal transaction. Of course, no prosecution was instituted against them. This is just another example of the unequal administration of our criminal law. There can be no doubt that the power and influence of the participants in this illegal transaction weighed heavily in the determination of the prosecuting officials not to proceed against them under the above cited authorities. We also find two justices of this court (see concurring opinions of Justices Schauer and Shenk) expressing their approval and commendation of the unlawful conduct of these participants in the consummation of this illegal transaction. This demonstrates the truth of the charge made by some critics of our judicial system that those with sufficient wealth, power and influence can evade the law and that the phrase "equal justice under law" is empty and meaningless in such situations. It is obvious that on the record before us justice has been outraged by the result reached by the majority and those who believe in the ideal of "equal justice under law," as well as the victims of this travesty, will look for an explanation. In my considered opinion it may be found only in the inferences which may be drawn from the time honored epigrammatic expression that "You can't convict a million dollars."

The essential facts of the controversy here are really very simple: Company and Attorney (made up of the same membership so really one and the same person legally speaking) contracted with a majority of the membership of Exchange for the purchase of the assets of Exchange some of whose members refused to consent to the purchase and sale. The purchase price was *$1,018,539.07*. After a series of legal maneuvers (to be discussed hereinafter), instigated by Company, Exchange subscribers, the innocent victims of the swindle, are held legally entitled to only the sum of *$323,300.39*.

Company brought the original action for declaratory relief regarding the rights of subscribers of Exchange. The original action culminated in an estimated award to *Exchange* of *$1,895,347.07*. *Exchange appealed*. The District Court of Appeal reversed on the ground that the Agreement was illegal, void and of no effect, and directed that an accounting be had to determine the value of the "whole going business" of Exchange which had been, by means of the Agreement, illegally

taken over by Company. *Company*, believing it had *lost* in the District Court of Appeal, petitioned this court for a hearing. We *denied* a hearing. The opinion of the District Court of Appeal (117 Cal.App.2d 519 [256 P.2d 677]) thereby became the law of the case on a retrial of the action.

On retrial Exchange recovered *$323,300.39* as the value of their "whole going business" which had been illegally taken over by Company as compared with the sum of *$1,895,347.07* recovered by it at the first trial from which judgment *Exchange* had appealed and won a reversal. The judgment rendered on the second trial was appealed by Exchange and determined by the same District Court of Appeal which had heard the first appeal. On the second appeal ((Cal.App.) 301 P.2d 112) the judgment was again reversed with the District Court of Appeal holding that the decision theretofore rendered by it had not been followed by the trial court and stating, among other things, that because of the judgment on retrial "the Company will have in fact everything, for which it agreed in the invalid agreement to pay considerably more than one million dollars to the subscribers and will pay for it only $323,300.39."

At the time of the second trial the evidence showed indisputably that Company had collected over 20 million dollars in gross premiums because of the increased business it had obtained through the illegal take-over of Exchange. The net profit was not ascertained. The District Court of Appeal specifically held, on the first appeal, that by means of the illegal agreement Company increased its clientele. It was there held that by its illegal agreement "the Company acquired the whole business of Exchange as a going concern and would therefore benefit by the increase of its clientele." Consents to the illegal agreement were obtained by sending out, in addition to 80 or 90 solicitors of consents, a letter which read, in part: "At normal expiration of your policy, in 1949 you will be offered a participating policy in Industrial Indemnity Company, a stock company. . . . Your policy with Industrial Indemnity Company will be serviced by the same personnel, located at the same offices as in the past." The District Court of Appeal (117 Cal.App.2d 519 [256 P.2d 677]) commented on Company's tactics as follows: "That *in this manner* the Company received an advantage not consistent with the position of a mere liquidator seems obvious."

By the holding of the majority here, Company profits by its illegal conduct in that it is permitted to:

1. Retain all the net profits directly traceable to former

Exchange subscribers although the loss experience was deducted from Exchange's recovery;

2. Retain the special surplus fund of *$592,322.31* and the increment thereof to which it was not entitled since Exchange was not in liquidation but had been illegally put out of business by Company and since the original underwriters' agreements were no longer in existence;

3. Retain the Attorney-in-Fact fees which amounted, at the time of trial, to $324,751.07 to which it was not entitled since the original underwriters' agreements were no longer in existence but were superseded by the illegal agreement.

In the majority opinion the issue as to net profits is discussed and the discussion relative thereto consists of quoting thirteen findings of fact and then making the bald, unadorned statement that "It logically follows that since the trial court's findings were supported by evidence and covered the issue that the appellate court had ordered to be retried, the judgment in the principal amount should be affirmed."

A slight attempt is made in the majority opinion to show that these findings are supported by the evidence in that certain testimony is quoted to the effect that since the policies were renewed annually there was no assurance that Exchange would have had *any* future subscribers had it not been illegally put out of business. Inasmuch as the record, as the majority admits, shows that Exchange had been the largest company of its kind for a great number of years prior to being illegally put out of business by Company, the theory behind the majority opinion that Exchange would probably not have continued in business in any event is nothing short of ridiculous. Absolutely no attempt is made in the majority opinion to reconcile the findings made by the trial court with the law of the case as set forth by the District Court of Appeal in its first opinion (117 Cal.App.2d 519 [256 P.2d 677]). Isolated bits of testimony extracted from the enormous record before us in support of erroneous findings do not concern us, or should not concern us, when there is a question of law involved. *We are not concerned with whether or not the evidence supports these erroneous findings and conclusions since it is obvious that the trial court was not following the law of the case as laid down by the decision of the District Court of Appeal, supra.* The very fact that the trial court considered Exchange to be in liquidation shows the error, since liquidation is the antithesis of a going business concern. It is also obvious that the judgment permitting Company to obtain all assets of Exchange for a lesser figure than that provided for

in the void Agreement is in contravention of the holding of the District Court of Appeal that Company and Attorney stood in a fiduciary relationship so far as Exchange was concerned and that a fiduciary may not benefit by a breach of its duties to its beneficiary. The District Court of Appeal specifically held in its first opinion (117 Cal.App.2d 519 [256 P.2d 677]) that the doctrine of corporate opportunities was applicable; that if a corporate officer or director seized for himself such opportunities "in violation of his fiduciary duty the corporation may claim for itself *all benefits so obtained by him*" (emphasis added) 117 Cal.App.2d at p. 533) and that the purchase of Exchange constituted the breach of Company-Attorney's fiduciary duty to Exchange subscribers. This court held in *Estate of Baird*, 193 Cal. 225, 258 [223 P. 974], while discussing the law of the case as decided in a former appeal in the same case, that "It was no part of the trial court's function to determine whether the former appeal had been correctly decided; its sole duty was to follow without question the principles established by that decision. This the trial court failed to do, and the instructions we have condemned are therefore prejudicially erroneous within the meaning of the constitution (sec. 4½, art. VI)." We also held (*Central Sav. Bank of Oakland* v. *Lake*, 201 Cal. 438, 443 [257 P. 521]) that "It has long been the law of this state that an unqualified reversal remands the cause for a new trial (*Falkner* v. *Hendy*, 107 Cal. 49, 54 [40 P. 21]), and places the parties in the trial court in the same position as if the cause had never been tried, *with the exception that the opinion of the court on appeal must be followed so far as applicable* (*Sharp* v. *Miller*, 66 Cal. 98 [4 P. 1065]; *Estate of Pusey*, 177 Cal. 367 [170 P. 846])." (Emphasis added.) (See also *Wells* v. *Lloyd*, 21 Cal.2d 452, 457 [132 P.2d 471]; *Chamberlain Co.* v. *Allis-Chalmers Mfg. Co.*, 74 Cal.App.2d 941, 943 [170 P.2d 85]; *Steelduct Co.* v. *Henger-Seltzer Co.*, 26 Cal.2d 634, 643 [160 P.2d 804]; *Wallace* v. *Sisson*, 114 Cal. 42, 43 [45 P. 1000]; *Porter* v. *Muller*, 112 Cal. 355, 366 [44 P. 729]; *Clark* v. *Deschamps*, 109 Cal.App.2d 765 [241 P.2d 681].)

We are not here concerned with the method by which Exchange's recovery should be determined since that is a matter to be determined on a retrial upon evidence given by experts in the insurance actuarial field. We are concerned here with what items should be considered a part of the subscribers' recovery.

Future Profits

In order to demonstrate conclusively that the findings do not follow the law of the case as set forth by the District Court

of Appeal, I will summarize that court's holdings and compare them with the trial court's findings:

1. The District Court held that the Transfer and Assumption Agreement constituted a *purchase* by Company of Exchange and that such Agreement was illegal and void. It was specifically held that Exchange was *not* in liquidation.

Finding IV recites that Underwriters hold the property and assets of Exchange "for distribution to the subscribers of the Exchange in *liquidation of its business and affairs*. . . ."

Company contended on the first appeal that the Agreement "was actually an agreement to liquidate." The District Court of Appeal said: "However, that is not the case. . . . Another circumstance which shows that the Company *did not act merely as liquidator* is of greater importance from a practical point of view. By taking over all assets, assuming all liabilities, including all outstanding policies of the Exchange and becoming directly liable thereon to the policyholders, the Company acquired the *whole business of the Exchange as a going concern and would therefore benefit by the increase of its clientele.*" (117 Cal.App.2d at 528, 529.)

2. The District Court of Appeal held the Transfer and Assumption Agreement illegal, void and of no effect.

Finding VI is to the effect that under the Agreement "no adjustment was to be made to Exchange with respect to the experience on the portion of the 1948 policies taken over thereunder; that because of the invalidity of the Agreement, the loss thereon must be charged up to Exchange." That loss experience amounted to *$156,600.53*.

Finding V recites that no policies written after December 31, 1948, for or on behalf of any former subscribers of Exchange form any part of the net worth of Exchange.

These findings are in direct conflict with the express holding of the District Court of Appeal that Company illegally and unlawfully took over the "*whole going business of Exchange.*"

Findings XIII and XIV are to the effect that policies of insurance were placed voluntarily with either Exchange or Company on a year to year basis and that all policies placed with Company after December 31, 1948, on behalf of persons who had formerly been policyholders of Exchange were voluntarily placed with Company as new items of business by insurance agents who were free to place such policies with such insurance carrier as they chose. Finding XIV concluded that no policy was placed with Company "by reason of or as a consequence of activities of Company being performed under, or arising as a consequence of, the Transfer and Assumption

Agreement or because Company was regarded in any sense as being the successor of Exchange."

The District Court of Appeal held firmly and unequivocally that due to Company's conduct in sending solicitors out and in mailing a letter to all Exchange subscribers it obtained an increase in its clientele to which it would not otherwise have been entitled.

Finding XVIII recites that Company did not use or receive any information from Exchange as a consequence of the illegal agreement.

Company had the information due to the interlocking relationship between it and Attorney and it was due to that information that it was able to contact all Exchange subscribers and obtain their business on the theory that the business placed with it would be serviced with the *same personnel and from the same offices* as it had been when Exchange was a going business concern. Furthermore, the solicitation and letters were both accomplished while Exchange was still a going concern.

Finding XXXI recites in effect that it is not true that Exchange was entitled to any future profits.

This of course directly belies the mandate of the District Court of Appeal that Company illegally took over the *whole going business of Exchange*; that an accounting should be had to determine the value thereof; that Company increased its clientele through its illegal tactics. *The evidence also showed indisputably that Company had collected over 20 million dollars in gross premiums due to the increased business it had obtained because of the illegal take-over of Exchange.*

The only effort made in the majority opinion to comply with the law of the case is to set forth the findings on the retrial and state without amplification that they are within the issue ordered to be retried and that they are supported by the evidence.

The District Court of Appeal (117 Cal.App.2d 519 [256 P.2d 677]) did *not* hold that Exchange was not entitled to the profits accruing by reason of the illegal take-over of its business by Company. It *did* hold that Exchange subscribers were not entitled to the profits made from *both* Exchange and Company business. The court had this to say (p. 539): "Under these circumstances it is not for us to say that the ultimate findings of the court below are necessarily improper inferences nor can we hold as a matter of law, contrary to said findings, that the Attorney *breached its fiduciary duty to*

subscribers when it engaged in the writing of workmen's compensation insurance through the medium of Company or that the business of Company was in equity the property of Exchange. We are the more satisfied that this result is not unjust because the gain by Exchange of all the profits of the business of Company without participation in them by any of Company's insureds would have given the subscribers of the Exchange a windfall wholly out of line with the setup of such Exchange." (Emphasis added.) The emphasized portion shows clearly that the District Court was referring to the *business* of *Company* as distinguished from the *profits made by Company from the business taken away from Exchange subscribers* since the statement was in answer to a contention made by Exchange that it was entitled to *all* of Company's business in the compensation insurance field before the unlawful take-over as well as all of its own business and the profits made therefrom after the take-over. This argument was based upon the theory that Company had breached its fiduciary duty by going into competition with Exchange in the compensation insurance field before the unlawful take-over.

As I have shown, *the findings do not comply with the law of the case* (117 Cal.App.2d 519 [256 P.2d 677]). Although I do not believe that the evidence *does* support the findings that were made, and certainly very little effort is made in the majority opinion to recite any of the evidence said to be sufficient, it is immaterial in any event since the findings are not in accord with the law of the case. The very fact that the trial court's findings and conclusions show, indisputably, that it considered that *Exchange was in liquidation* shows the error since liquidation is the antithesis of a going business concern. It is also obvious that the judgment permitting Company to obtain all assets of Exchange for a lower figure than that provided for in the void Agreement is in contravention of the holding of the District Court of Appeal that Company and Attorney stood in a fiduciary relationship so far as Exchange was concerned and that a fiduciary may not benefit by a breach of its duties to its beneficiary.

So far as business profits are concerned, the law is that where there has been a breach of a fiduciary duty, a constructive trust is imposed upon a person in order to prevent his unjust enrichment. In most cases where a constructive trust is imposed, the result is to restore to the injured person property of which he has been unjustly deprived and to take from the wrongdoer property, the retention of which by him, would result in a corresponding unjust enrichment of the

wrongdoer. (*Koyer* v. *Willmon*, 150 Cal. 785 [90 P. 135]; *Broder* v. *Conklin*, 121 Cal. 282 [53 P. 699]; *Johnson* v. *Clark*, 7 Cal.2d 529 [61 P.2d 767]; *Forman* v. *Goldberg*, 42 Cal.App. 2d 308 [108 P.2d 983]; Rest., Restitution, §§ 160, 190.) It follows logically from the foregoing that before Exchange may be made whole for what has been illegally taken from it by Company, the latter must be forced to return to Exchange that which was taken together with the profits made therefrom.

Exchange introduced evidence showing that it was possible to trace former Exchange business for the five-year period subsequent to the execution of the illegal Agreement. The majority would have us assume that had the illegal Agreement not been executed all of Exchange subscribers would have ceased being Exchange subscribers and placed their business with Company. This assumption is neither logical nor probable; Exchange had been a prosperous going concern for many years prior to the execution of the Agreement and would, in all probability, have continued as one. The majority holding that Exchange subscribers are entitled to no reimbursement from Company after the expiration of the last yearly policy issued by Exchange is a judicial sanction of something which the law has always abhorred—*that a wrongdoer be permitted to profit from his own wrong.*

Company-Attorney stood in a fiduciary relation to Exchange (117 Cal.App.2d 519 [256 P.2d 677]) and should therefore be held to the same standards as the law imposes on the trustee of an express trust (117 Cal.App.2d 519 [256 P.2d 677]). (See also *Clapp* v. *Vatcher*, 9 Cal.App. 462, 466 [99 P. 549]; *Edgar* v. *Bank of America*, 50 Cal.App.2d 827, 833 [123 P.2d 885]; The Fiduciary Principle, 37 C.L.R. 539-555.) It is an elementary principle of the law of trusts that a trustee is forbidden to make use of the trust property for his private or individual purposes or to derive any profit therefrom (Civ. Code, § 2229; *Purdy* v. *Johnson*, 174 Cal. 521, 529 [163 P. 893]; Rest., Trusts, § 205(b); *Crenshaw* v. *Roy C. Seeley Co.*, 129 Cal.App. 627 [19 P.2d 50]; 25 Cal.Jur., § 190, p. 342) and if he does derive profit from such a breach of trust he is liable to the beneficiary therefor (*Estate of Piercy*, 168 Cal. 755 [145 P. 91]; *Burns* v. *Clark*, 133 Cal. 634, 639 [66 P. 12, 85 Am.St.Rep. 233]; *Tobin Grocery Co.* v. *Spry*, 204 Cal. 247 [267 P. 694]; 2 Scott on Trusts, § 170.2, p. 1199; Rest., Trusts, § 205(b); Civ. Code, § 2237). The policy of the law has always been, up until this case, to put fiduciaries beyond the reach of temptation by making it unprofitable for them to yield to it. (*MacIsaac* v. *Pozzo*, 81 Cal.App.2d 278, 285 [183 P.2d 910];

Miller v. *McKinnon,* 20 Cal.2d 83 [124 P.2d 34, 140 A.L.R. 570]; *Hoyt* v. *Hampe,* 206 Iowa 206 [214 N.W. 718, 724].) The breach of the fiduciary duty in the case at bar has proved *very* profitable to Company and a majority of this court has placed its stamp of approval thereon.

The rule which *should* be applied here is that stated in the Restatement of Restitution, section 160, Comment (d): "There are some situations, however, in which a constructive trust is imposed in favor of a plaintiff who has not suffered a loss or who has not suffered a loss as great as the benefit received by the defendant. In these situations the defendant is compelled to surrender the benefit on the ground that he would be unjustly enriched if he were permitted to retain it, even though that enrichment is not at the expense of the plaintiff. Thus, if the defendant has made a profit through the violation of a duty to the plaintiff to whom he is in a fiduciary relation, he can be compelled to surrender the profit to the plaintiff, although the profit was not made at the expense of the plaintiff." The following cases from California* which are in accord with the Restatement rule just set forth must, under the majority holding, be deemed overruled. The majority opinion, however, in totally ignoring the facts, the law of the case, and the far-reaching effects its ill-advised decision will have on one of California's major industries, does not even discuss the law of restitution, and trusts, but holds, simply and without amplification, that the evidence supports the findings! One would never know from reading the majority opinion that any law was involved; one would never know the enormity of the theft committed as the result of the unlawful conduct of the officers of Company which is here judicially sanctioned.

Special Surplus Fund

In order that the attorneys *and* the people of this state who are interested in the purchase of insurance may understand just exactly what took place in this case, I will set forth the facts relating to the second major issue involved here.

The undisputed evidence in the record shows that under the old underwriters' agreements which were the original

*Burns v. Clark, 133 Cal. 634 [66 P. 12, 85 Am.St.Rep. 233]; *Tobin Grocery Co.* v. *Spry,* 204 Cal. 247 [267 P. 694]; *Weiner* v. *Mullaney,* 59 Cal.App.2d 620 [140 P.2d 704]; *Edgar* v. *Bank of America,* 102 Cal.App.2d 700 [228 P.2d 21]; *Lantz* v. *Stribling,* 130 Cal.App.2d 476 [279 P.2d 112]; and see also *Crites, Inc.* v. *Prudential Co.,* 322 U.S. 408, 417 [64 S.Ct. 1075, 88 L.Ed. 1356]; *Magruder* v. *Drury,* 235 U.S. 106, 120 [35 S.Ct. 77, 59 L.Ed. 151]; *Jackson* v. *Smith,* 254 U.S. 586, 588-589 [41 S.Ct. 200, 65 L.Ed. 418].

agreements between Exchange and Attorney, the Special Surplus Fund was a fund set aside from premiums on policies issued by Exchange and was intended to be used for the expenses of liquidation in the event Exchange was ever liquidated by Attorney in accordance with the terms of the original agreements. There is no dispute that such liquidation has *never* taken place or was even contemplated, as the undisputed evidence shows that Company took over all assets of Exchange as a *going business* and that the Special Surplus Fund was one of the items which Company set up as an asset of Exchange for which Company agreed to pay the subscribers of Exchange the sum of $1,045,159.71. How the trial court determined that Company was entitled to retain this Special Surplus Fund is one of the mysteries which the record does not reveal. It was an asset derived from the premiums on policies issued by Exchange and was set aside for a specific purpose for which it was never used, hence it must still be an asset of Exchange. This Special Surplus Fund at the time of the illegal take-over by Company amounted to $592,322.31 and the record shows that it was increased between January 1, 1949, and March 31, 1954, by the accrual of $119,307.37, so that on the last-mentioned date it amounted to the sum of $711,621.68.

The majority holding is, of course, that Company is entitled to this fund. The theory relied on is a marvelous example of utter confusion. First it is said: ". . . the trial court found that the Special Surplus Fund was, under the Underwriters Agreement,† to be reserved for expenses incurred in connection with *liquidation* and payable to Attorney; that on November 15, 1953, this was assigned to Company as compensation for work heretofore performed in connection with the *liquidation* of Exchange, less such portion as required to reimburse Attorney for future costs of *liquidation*; and that the subscribers have no right or claim to this surplus since it was not a part of Exchange's business or assets." (Emphasis added.) Having quoted the provisions of the superseded underwriters' agreements, the majority then states: "Under the Underwriters Agreement, Attorney-in-Fact was entitled to this fund 'if Exchange discontinues business,' as compensation for winding up the affairs and liquidation. The question then arises whether Exchange has been 'discontinued.' The trial court found that it had, and the evidence supports the finding." It should be carefully borne in mind that this Special Surplus Fund was *derived from investment income of Exchange*. It should also be remembered that the member-

†More of this later.

ship of Company and Attorney was identical. It should also be remembered that the District Court of Appeal specifically and unequivocally held that Exchange was *not in liquidation. Under the majority holding, the involuntary discontinuance of business by Exchange because of the machinations of Company must be paid for by Exchange.*

Relying on the illegal and void Transfer and Assumption Agreement the majority quote from its provisions that the Attorney waived its right to the Special Surplus Fund. And even though the Special Surplus Fund was one of the assets of Exchange for which Company contracted (Transfer and Assumption Agreement) to pay Exchange the sum of $1,045,159.71, the majority state that "The court found, and the evidence amply supports the finding, that future profits, Attorney fees and the Special Surplus Fund were not items obtained by Company as a consequence of the illegal Transfer and Assumption Agreement." The public is also informed that the subscribers of Exchange "have not suffered either injury or damage" even though they have been cheated out of over a half million dollars. It is held that since the trial court found that Company had not waived its right to this Special Surplus Fund and that since Attorney was originally entitled to it for expenses of liquidation and that Attorney, through the void Transfer and Assumption Agreement had waived its rights thereto, Company was legally entitled to the fund. When the facts are understood it becomes apparent that Attorney's waiver of its rights to the fund is exactly the same as a man transferring his money from his right to his left trouser pocket. The majority opinion does not make clear just how the terms of an agreement declared by the District Court of Appeal to be void and of no effect can be relied on in support of a holding of the superior court. The majority, in an effort to justify its holding, quotes, out of context, a statement made by the District Court of Appeal in its opinion on the first appeal (117 Cal.App.2d 519, 537 [256 P.2d 677]) that "The Company did not at any time in the operation of its business use any funds, facilities or information belonging to, or secured through, the Exchange." In reality the District Court was referring to the situation as it was *prior to* the illegal take-over of Exchange when Company engaged in writing compensation insurance in competition with Exchange.

The majority, in giving everything involved to Company, goes along with Company's argument that it was entitled to the Special Surplus Fund under the old underwriters' agree-

ments which, it contends, were reinstated by the holding of the District Court of Appeal that the Transfer and Assumption Agreement was invalid and void. The underwriters' agreements provided only that Company should use the fund in the event of the *voluntary* discontinuance of business by Exchange. The result to be reached so far as the Special Surplus Fund is concerned *should be*, since Exchange was illegally sold to Company and since it is now too late to set aside the illegal sale, that the subscribers of Exchange should be compensated as nearly as possible for that which they have lost which includes this fund which constituted their investment earnings. It stands to reason that had the illegal sale not taken place, the Special Surplus Fund would have remained intact. Exchange agrees, although under the circumstances its agreement is a magnanimous one, that Company should be reimbursed for its *actual* expenses in winding up the affairs of Exchange. But aside from that agreement, Exchange is most definitely entitled to the Special Surplus Fund. (See *Schwarting* v. *Artel*, 40 Cal.App.2d 433, 441 [105 P.2d 380]; *Woods* v. *City Nat. Bank & Trust Co.*, 312 U.S. 262, 269 [61 S.Ct. 493, 85 L.Ed. 820].)

Attorney-in-Fact Fees

This is another major issue involved which the majority opinion glosses over, and again the facts relating thereto will be set forth.

Prior to the execution of the Agreement and *under the old underwriters' agreements* Attorney was entitled to retain 25 per cent of the premium deposits and 5 per cent of dividends as its fee. In consideration of this fee, Attorney was required to pay for all offices, equipment and personnel used for the business of Exchange. Subsequent to January 1, 1949, when the illegal Agreement became effective, Company admits that it handled this business for its own account. The evidence shows that Company had, at the time of retrial, collected *$78,419.13* as fees on dividends and the sum of *$246,331.94* as fees on premiums on the business directly traceable to former Exchange subscribers. Just how, or why, Exchange should be charged with the fees provided for by the old underwriters' agreements after the effective date of the illegal Agreement remains a mystery. After the effective date of the illegal Agreement *by Company's own admission it was acting on its own account and there was no Attorney in existence.* Exchange's recovery should be lessened *only* by the amount of the *actual* costs incurred by Company in conducting the business directly traceable to former Exchange subscribers. To hold

otherwise permits Company to profit by its own wrongdoing. There can be no question but that the old underwriters' agreements were superseded by the illegal Agreement; there can also be no question but that the old underwriters' agreements were not revitalized by the District Court of Appeal's holding that the Transfer and Assumption Agreement was illegal, void and of no effect. Company by its conduct after the assumption of Exchange business demonstrated that it was not acting under the old underwriters' agreements. (See *Pennsylvania Water etc. Co.* v. *Consolidated Gas etc. Co.* [C.A. 4, 1951], 186 F.2d 934, and *Virginia Dare Transp. Co.* v. *Norfolk Southern Bus Corp.* [C.A. 4, 1949], 176 F.2d 354, for cases holding that a judicial declaration of the invalidity of a later contract does not revitalize an original valid contract.)

The findings of the trial court with respect to the fees paid the Attorney-in-Fact are commented on as follows by the majority: "The evidence supporting the foregoing findings is: (a) the Underwriters Agreement; (b) the Transfer and Assumption Agreement; and (c) the agreement whereby Company assumed the obligations of Attorney and Attorney assigned its rights to the management fees." This statement is particularly interesting when it is remembered (1) that the Underwriters' Agreement was superseded by the Transfer and Assumption Agreement which was held to be illegal, void and of no effect, and (3) that the "agreement" between Attorney and Company was an agreement made by one legal entity with itself. I cannot conceive of a majority of this court sanctioning the use of a void and illegal contract as evidence in a case which arose out of that particular void contract. But by its holding here a majority of this court not only judicially sanctions an obvious wrong, but, in effect, allows the wrongdoer to retain both the fruits of his wrong, a bonus for his wrongdoing, and his expenses incident thereto!

Conclusions

We have this case before us because of the holding of the District Court of Appeal (117 Cal.App.2d 519) that the Agreement was illegal, void and of no effect because it was in violation of section 1101 of the Insurance Code. Section 1106 of the same code makes any violation of section 1101 a misdemeanor. The District Court of Appeal held that the Agreement, since it was made contrary to the terms of a law designed for the protection of the public and which prescribed a penalty for its violation, was illegal, void and of no effect.

There can be no question but that the same rule of law

should be applied here as this court, speaking through Mr. Justice Shenk, applied in the case of *Contractor's etc. Assn.* v. *California Comp. Ins. Co.*, [1]48 Cal.2d 71, 76 [307 P.2d 626], and which was a unanimous decision. It was there held: "Acceptance or receipt of an unlawful rebate is a misdemeanor. (Ins. Code, § 752.) Violation of the minimum rating law is also a misdemeanor. (Ins. Code, § 11742.) This court said in *Severance* v. *Knight-Counihan Co.*, 29 Cal.2d 561 (*supra*), at page 568: 'It is settled that a contract must have a lawful object (Civ. Code, §§ 1596, 1598, 1599) and that a contract for an object prohibited by a penal law is void. . . . "The general rule controlling in cases of this character is that where a statute prohibits or attaches a penalty to the doing of an act, the act is void, and this, notwithstanding that the statute does not expressly pronounce it so, and it is immaterial whether the thing forbidden is *malum in se* or merely *malum prohibitum*. . . . The imposition by statute of a penalty implies a prohibition of the act to which the penalty is attached, and a contract founded upon such act is void." ' " Applying the foregoing rule to the facts of the case at bar, we have a situation where Company by means of a contract "having an object prohibited by a penal law" acquired the property and assets of Exchange. That contract was illegal and void because the act of entering into it constituted a crime. Such being the case the subscribers of Exchange should have the right to recover everything of value which Company acquired under such illegal and void contract together with the increment thereof.

The judgment in this case should, in the interest of justice, be reversed with directions to the trial court which cannot be misunderstood. Such directions should encompass all the issues raised and should be for an accounting to determine:

1. The net profits made by Company from business directly traceable to former Exchange business. The trial court should retain jurisdiction so that the net profits accruing from year to year which are directly traceable to Exchange business may be judicially ascertained and awarded to Exchange subscribers;

2. The Special Surplus Fund comprising the investment earnings of Exchange *prior* to its illegal take-over by Company and amounting at the time of trial to the sum of $711,769.68 should be awarded to Exchange subscribers together with the increment thereof.

[1]Advance Report Citation: 48 A.C. 67, 72.

3. The Attorney-in-Fact fees, amounting to the sum of $324,751.07, at the time of retrial, should be awarded to Exchange subscribers. The direction to the trial court to ascertain the *net* profits attributable to Exchange business would allow Company its actual expenses in conducting the business directly traceable to former Exchange subscribers.

I agree that the awarding of, or refusal to award, interest on unliquidated amounts is a matter generally held to be discretionary with the trial court (*Title Ins. & Trust Co.* v. *Ingersoll*, 158 Cal. 474 [111 P. 360]; *Wheeler* v. *Bolton*, 92 Cal. 159 [28 P. 558]; *Leonard* v. *Huston*, 122 Cal.App.2d 541 [265 P.2d 566]; *Stockton Theatres, Inc.* v. *Palermo*, 121 Cal.App.2d 616 [264 P.2d 74]).

I agree that appellant Johnson is a mere intervener in the stockholders' derivative action and that it may not participate in the presentation of the main case except as counsel for the main stockholders may consent or the court may permit. It appears here that appellant Johnson's rights were fully protected by counsel for the main stockholders (*Mann* v. *Superior Court*, 53 Cal.App.2d 272, 280 [127 P.2d 970]).

For the reasons heretofore set forth it should be clear to every thinking person that the judgment should be reversed with clear directions to the trial court for its guidance on the retrial.

MINUTES

San Francisco, Oct. 28, 1957.

In Bank.

S F 19854 (1st Civ 17998) — Nomm v. Nomm. The above entitled appeal is transferred to the District Court of Appeal, First Appellate District.

S F 19855 (1st Civ 17964)—Rousseau v Hurtado. The above entitled appeal, now pending in the District Court of Appeal, First Appellate District, is transferred to the Supreme Court and retransferred to the District Court of Appeal, First Appellate District.

L A 24778—Bolen v. Bolen. The above entitled appeal is transferred to the District Court of Appeal, Second Appellate District.

— (2d Civ 22818) — Jeffrion v. Jeffrion. The above entitled cause and motion noticed therein, now pending in the District Court of Appeal, Second Appellate District, are transferred to the Supreme Court and retransferred to the District Court of Appeal, Second Appellate District.

Sac 6872 — Estate of Antwerp. The above entitled appeal is transferred to the District Court of Appeal, Third Appellate District.

— (3d Civ 9399) — Dicker v. West. The above entitled appeal, now pending in the District Court of Appeal, Third Appellate District, is transferred to the Supreme Court and retransferred to the District Court of Appeal, Third Appellate District.

APP.

B

[Civ. No. 15023. First Dist., Div. Two. Apr. 30, 1953.]

INDUSTRIAL INDEMNITY COMPANY (a Corporation) et al., Respondents, v. GOLDEN STATE COMPANY, LTD. (a Corporation), et al., Appellants; THE ROBERT L. JOHNSON CORPORATION (a Corporation), Intervener and Appellant.

Note

Pages 520 and 521 are not present

APPEAL from a judgment of the Superior Court of the City and County of San Francisco. Daniel R. Shoemaker, Judge. Reversed with directions.

Action for declaratory relief. Judgment for plaintiffs reversed with directions.

NOURSE, P. J.—This appeal relates to an action for declaratory relief regarding the rights of subscribers of Industrial Indemnity Exchange, a reciprocal insurance exchange, having as its field workmen's compensation insurance, hereinafter called "Exchange," under an agreement by which the business of said Exchange was transferred as a whole to Industrial Indemnity Company, an insurance corporation, hereinafter called "Company," for a price to be distributed to subscribers, and to cross-actions in behalf of said subscribers claiming mainly that all of the insurance business transacted by Company belonged in equity to Exchange, from whose business it was alleged to have been disloyally diverted by Industrial Underwriters, a partnership, the attorney-in-fact of said Exchange, hereinafter called the "Attorney" whose partners substantially owned the stock of Company.

A reciprocal insurance exchange, regulated in sections 1280-1530 of the Insurance Code, is an unincorporated business organization of a special character in which the participants, called subscribers (or underwriters) are both insurers and insureds; for their mutual protection, they exchange insurance contracts through the medium of an attorney-in-fact, empowered in each underwriters agreement not only to exchange insurance contracts for the subscribers, but also to exercise

all other functions of an insurer, e. g., to set rates, to settle losses, to compromise claims, to cancel contracts. The subscribers furnish by their premium deposits, the means required for losses and costs, reserves and surpluses of the reciprocal insurance of them all, and therefore are entitled to the equity in the assets of the Exchange subject to the purpose for which they have furnished said means. If the amount of premiums deposited is not fully required for the purposes mentioned, the excess, called savings, is returned in whole or in part as dividends. The attorney-in-fact receives a sizable percentage of the premiums deposited in consideration of which he does not only provide his own services, but also has to defray many of the costs of the business. In this case the Attorney, from the 17½ per cent of the premium deposits to which it was contractually entitled, had to provide and to pay for all offices, equipment and personnel required for the business of Exchange. The affairs of a reciprocal insurance exchange are normally supervised to some extent, and they were in this case, by an advisory commission which represents the subscribers and whose powers and formation are regulated in the underwriters agreements.

The matters now before this court found their origin in objections made in 1947-1948 by the Insurance Commissioner of the State of California to certain interrelations allegedly existing and certain transactions allegedly having taken place between Exchange, Attorney and Company. After some time the objections were embodied in two unsigned and undated drafts entitled "Accusations," which culminated in the conclusion that the stated acts constituted ground for suspension or revocation of the certificates of authority of the Exchange or of Exchange and Company but which were expressly stated to be meant only as a basis of discussion. The main points raised related to the following alleged facts: The stock interest of the members of the Attorney in Company, a Corporation competing with Exchange in the field of workmen's compensation insurance and the existence of interlocking functions between them; the farming out since 1946 by the Attorney to Company of the performance of substantially all of the duties for which Exchange paid the Attorney, whereas the Attorney retained 20 per cent of the compensation received from Exchange; the segregation under the underwriters agreements in a special surplus fund of all investment income of the Exchange to serve in case of liquidation of Exchange as compensation for the activities and costs of

the Attorney in that respect; the reinsurance by Exchange since 1945 of the larger participating insurance policies written by Company and the treatment of said reinsurance business as normal reciprocal business of Exchange; the reinsurance by Company from 1939 until 1941 of possible assessment liability of the subscribers of Exchange at a premium considered excessive by the Commissioner. Long negotiations followed. The Commissioner originally took the position that there should be a complete separation of the interrelation objected to. The Attorney and the Company thought this unacceptable and maintained that all they had done was proper under existing law, agreements and circumstances (their said position was later generally sustained in the findings herein). However, in principle an agreement with the Commissioner was reached on the basis of the following plan: Company would as of January 1, 1949, take over all assets, assume all liabilities, take over and reinsure all policies of Exchange, and pay in the course of time to subscribers of Exchange an amount in cash which would as closely as possible equal the entire net worth of Exchange. To eliminate the necessity of basing on estimates elements of the net worth, such as liability for claims, unbilled earned premiums, and accrued dividends on policies, the Company would run out the business of Exchange as it existed at the end of 1948 for a maximum of three years and adjust the estimated amounts of such items in accordance with the actual results. The cash amount so obtained would, subject to change in the manner of distribution if a final court decision required a different manner, be distributed to those who were subscribers of Exchange on December 31, 1948, in proportion to the total earned premium of such subscribers with Exchange during the period 1931-1948, each subscriber receiving a minimum of $50. The Company and the Attorney made the following concessions with respect to some matters stated above as objected to by the Commissioner: The Attorney waived its right to the special surplus fund as compensation for liquidation activities, Company, with certain stated exceptions, to bear the costs of running out the business of Exchange; Company and Exchange agreed to terminate and reverse the reinsurance by Exchange of participating policies of Company from the beginning so that Company would not participate in the distribution to subscribers under the plan; to correct the amount of premium paid for the 1939-1941 reinsurance of assessment liability of subscribers of Exchange, said insur-

ance was made retroactively participating to the extent of 99½ per cent of the premium paid, which percentage would be refunded.

The Commissioner and the Attorney were both of the opinion that an agreement in accordance with the plan needed the consent of the subscribers of Exchange. After a summary of the plan with a letter of the Advisory Commission advising its adoption had been handed to all subscribers, approximately 98 per cent of them both according to number and premium volume signed written consents. On December 21, 1948, a written transfer and assumption agreement was executed to effectuate the plan stated above; the Commissioner approved it and on January 1, 1949, Company took over in accordance with said agreement.

Following a suggestion of the commissioner those in favor of the agreement, the Exchange, the Attorney, the Advisory Committee, three consenting subscribers in representative capacity and Company, brought this action for declaratory relief against all nonconsenting subscribers by name, praying for a declaration to the effect that past subscribers to the Exchange (no longer subscribers on December 31, 1948) have no interest in the net worth of Exchange, that the plan for distribution contained in the agreement is fair and that nonconsenting subscribers have no further rights than those given to them in the agreement. It will not be necessary to detail the pleadings of the several nonconsenting subscribers. They resulted in bringing before the court the defenses that the Attorney and the Advisory Committee had no authority to conclude the transfer and assumption agreement, that the consents of the Commissioner and subscribers were invalid because obtained by misrepresentations, that the transfer and assumption agreement was invalid as a fraudulent attempt by the Attorney to eliminate Exchange as a competitor of Company, that the transfer and assumption agreement did not give subscribers all that they were entitled to because it gave them neither the value of the goodwill of Exchange nor of the business of Company which belonged to Exchange on the ground that the Attorney and the Company of which it owned the stock had built up the business of Company in competition with Exchange in violation of the duty of the Attorney, and finally that methods of dissolution and distribution contained in the agreement were unfair. There was also before the court a cross-complaint of some nonconsenting subscribers in representative capacity asking a declaration that the assets and

business of Company as built up since May 3, 1939, belonged to the subscribers of Exchange and further a declaration of rights as to the different points in dispute.

Moreover Robert L. Johnson Corporation, a subscriber which had signed a consent but had served notice of rescission of said consent on the Attorney, had intervened and united as a defendant, assuming the defenses and cross-complaint set out above, urged the invalidity of the consent on the ground of insufficient information and, because of an alleged equivocal position of the Attorney, prayed moreover for an accounting as to all that rightfully belonged to Exchange, and the appointment of a conservator of the property in dispute and a rescission in full of intervener's consent. Cross-defendants urged against the cross-complaint of the nonconsenting subscribers certain affirmative defenses including the defenses of the statute of limitations and laches and as against intervener moreover the defense of ratification.

The court found in nearly all respects for the plaintiffs and against the cross-complainants; it found however against the above affirmative defenses of the cross-defendants. The judgment declared in substance that past subscribers had no interest in the Exchange and were not entitled to participate in any distribution; that the transfer and assumption agreement was fair and equitable, validly executed and binding on all past and present subscribers of Exchange, and that they had no right to any net worth or assets of Exchange except as provided in said agreement, that said agreement distributed to the subscribers all they were entitled to in the most equitable, reasonable and practical manner and that subscribers had no interest in the business or assets of Company. Judgment on the cross-complaints was for cross-defendants.

There are two separate main appeals, one from all of the judgment by three nonconsenting subscribers and one from all of the judgment except the part overruling cross-defendants' affirmative defenses by intervener and moreover there is a cross-appeal by cross-defendants as to said overruling of said affirmative defenses only. Over and above the points mentioned as having been before the trial court it was urged on appeal among other matters that the transfer and assumption agreement was unenforceable as a contract made by a trustee in his own behalf with respect to trust property, that intervener was erroneously barred from amending its pleadings so as to represent also other consenting

subscribers who might desire to rescind their consent and that there were certain inconsistencies in the findings.

We have concluded that the original action for declaratory relief should have been denied because the agreement to which it relates is void as violating section 1101 of the Insurance Code, expressly made applicable to reciprocal exchanges by section 1282 of said code. Section 1101 reads insofar as applicable to this case: "An admitted insurer's officers, directors, trustees and any persons who have authority in the management of the insurer's funds, shall not, unless otherwise provided in this code: . . . (c) Directly or indirectly purchase, or be interested in the purchase of, any of the assets of the insurer." Section 1106, Insurance Code, reads in part: "Any person violating . . . Sections 1101, . . . is guilty of a misdemeanor."

This exact point was not raised by any of the parties, but was briefed specially at the request of this court. **[1]** Nevertheless no action could be maintained on this agreement if it actually violated the code. "'[A] contract made contrary to the terms of a law designed for the protection of the public and prescribing a penalty for the violation thereof is illegal and void, and no action may be brought to enforce such contract . . . whenever the illegality appears, whether the evidence comes from one side or the other, the disclosure is fatal to the case.'" *Loving & Evans* v. *Blick*, 33 Cal.2d 603, 607 [204 P.2d 23].) **[2]** See for the rule that the court should on its own motion refuse to entertain the action when such illegality appears as a matter of law from the whole case before the court: *Union Collection Co.* v. *Buckman*, 150 Cal. 159, 165 [88 P. 708, 119 Am.St.Rep. 164, 11 Ann.Cas. 609, 9 L.R.A.N.S. 568]; *Endicott* v. *Rosenthal*, 216 Cal. 721, 728 [16 P.2d 673]; *Fewel & Dawes, Inc.* v. *Pratt*, 17 Cal.2d 85, 92 [109 P.2d 650]. Considering these authorities it cannot be denied, and it is not denied by respondents, that if the agreement violates section 1101, Insurance Code, it is void and unenforceable.

Neither is it denied nor could it be denied that the members of the Attorney are persons who have authority in the management of the funds of the Exchange. The interrelation between the Attorney and the Company, which is at the basis of this whole case, leaves no doubt that said partners in the Attorney would be interested in, at least indirectly, any purchase made by the Company. In this respect it will suf-

fice to quote from finding 16 of the court the following passus which is not attacked:

"The stock ownership of Industrial Indemnity Company has at all times been substantially the same as the ownership of Industrial Underwriters, a partnership, the attorney-in-fact of the Exchange."

[3] However respondents contend that the agreement was not a beneficial sale of assets to the Company as prohibited by section 1101 but a transfer for the purpose of liquidating only. We do not agree. The amended complaint in paragraphs XXVII and XXXIII refers to *sale* and *selling* of all assets. The "Transfer and Assumption Agreement" provides among other things:

"Effective 12:01 A. M. January 1, 1949, Exchange will *sell*, assign and transfer and it does hereby *sell*, assign and transfer to Company all of the assets of the Exchange. . . ." (Emphasis ours.)

"As compensation for the assignment and transfer to it of the assets of the Exchange, Company will pay . . . an amount equal to the 'adjusted net worth' of the Exchange, computed as follows:"

The provisions are then to the effect that first the net worth of the Exchange (including the reserve for contingencies, special surplus and unassigned surplus) is determined according to an audited balance sheet as of December 31, 1948, on which all assets are valued at market value as of December 31, 1948; thereafter adjustments are made in many items of that balance sheet on the basis of the actual results obtained during the running out of the business of the Exchange during three years. If all items on the balance sheet were adjusted according to the results of the running out, all assets were liquidated during those three years and nothing whatever would remain as advantage to the Company, it could be said that nothing was actually purchased by the Company and that notwithstanding the word "sell" used in the agreement the transaction was actually an agreement to liquidate. However that is not the case. No adjustment is provided for the investments. On the balance sheet as of December 31, 1948, which is in evidence as Plaintiffs' Exhibit 80, there appear United States government obligations for $3,175,000. They are acquired by the Company at that price without any adjustment or duty to account for their liquidation. Although the purchase takes place at market value it is nevertheless a violation of section 1101, Insurance Code, which prohibits

any purchase of assets of the insurer by its managing officers and which in that respect differs from section 421a, Civil Code, which governed the subject prior to the enactment of the Insurance Code and which prohibited such purchases only if made "for a less sum than the current market value." Said change must have been deliberate and the provision of section two of the Insurance Code that provisions substantially the same as preexisting provisions will be construed as restatements thereof has no application.

Another circumstance which shows that the Company did not act merely as liquidator is of greater importance from a practical point of view. By taking over all assets, assuming all liabilities, including all outstanding policies of the Exchange and becoming directly liable thereon to the policyholders, the Company acquired the whole business of the Exchange as a going concern and would therefore benefit by the increase of its clientele. Characteristic in this respect is the following passus from the document sent by the Advisory Committee to subscribers on November 29, 1948, setting out and recommending acceptance of the proposed plan:

"At normal expiration of your policy, in 1949, you will be offered a participating policy by Industrial Indemnity Company, a stock company. . . . (b) Your policy with Industrial Indemnity Company will be serviced by the same personnel, located at the same offices as in the past." That in this manner the Company received an advantage not consistent with the position of a mere liquidator seems obvious. The findings show that the Commissioner was also of this opinion. We find in finding 47 that it was the position of the Insurance Commissioner at the outset of the negotiations, that the amount to which subscribers were entitled should include "an amount representing a reasonable going concern value of the Exchange as measured by the value to the Company of any Exchange business it might take over in the event of consolidation. . . .

"The Insurance Commissioner thereafter concluded that any business taken over by the Company in the event of consolidation of Company and Exchange would not result in any profits to Company greater than the profit then being made by the attorney-in-fact of the Exchange, that the profit being made by the attorney-in-fact of the Exchange did not belong to the subscribers at the Exchange, and thereafter abandoned his position that any amount should be paid or recognized as representing going concern value of the Exchange." If the Attorney would lose as much as the Company would win,

there might, considering their identical ownership, be good reason for the Commissioner not to persist in his demand of separate payment for going concern value, but his original demand and the reason given for his desisting show his conviction that the Company would obtain business from the Exchange which would be of value for the Company, and even if the concessions made by the Company and the Attorney, stated hereinbefore, would sufficiently compensate the subscribers for said advantage received by the Company, that would not alter the fact that the Company was not only liquidator but beneficially acquired at least the investments and the going business. The fact that during the years 1946, 1947 and 1948 more premium was returned to subscribers of Exchange than was in accord with the actual business results of these years (finding 66) does not show that the acquisition of the large going business of Exchange was not valuable to Company.

Respondents urge, however, that even if it were an actual sale, as we consider it, the agreement would come under an exception to section 1101 contained in section 1105, reading: "This article shall not prevent: (a) The purchase by any person of any asset which the commissioner requires to be sold, at a price approved by the commissioner." The contention is without merit. The Commissioner did not require and had no power to require the sale of the whole business of the Exchange as a going concern. [4] To "require" in this sense means "to demand; to claim as by right and authority; to exact." (Webster.) The Commissioner did not demand it and had no authority to demand it. Respondents' contention is based on the fact that the Commissioner threatened suspension or revocation of the certificates of authority of Exchange and Company if his objections to the interrelation of the Attorney and the Company and other matters stated in the "Accusations" would not be remedied to his satisfaction. However, it is not true that the remedy he primarily wanted or which he required was the taking over of the Exchange by the Company. The court found (in finding 47): "The preferred plan of the Commissioner was one of separation." In the Statement of the Exchange of November 29, 1948, outlining principal terms of the plan, it is said that the discussions with the Commissioner revealed "that the problems presented might be solved either by a complete separation of the two organizations, or by a merger of Industrial Indemnity Exchange and Industrial Indemnity Com-

pany upon the terms herein set forth. Upon giving thorough consideration to both of these possibilities, it was found that the first alternative was not acceptable to the attorney-in-fact and the Company. . . . *The representatives of the Insurance Commissioner have stated that when this plan is formally submitted to the Commissioner, they will be inclined to recommend its approval.*" The above quotations show that the transaction was not authoritatively demanded by the Commissioner but preferred by the Attorney and the Company and approved by the Commissioner. This is also shown by the requirement of approval by subscribers. It is said in respondents' brief (pp. 120-121): "It was the position of the Commissioner of Insurance that it [the agreement] would have to be approved by a majority of the policyholders. . . . On the other hand, respondents felt that the agreement should have the approval of more than a bare majority of the policyholders and the agreement was drawn up on the basis of approval of two-thirds of the policyholders." The necessity of approval of policyholders is inconsistent with a transaction demanded by the Commissioner as of right.

Moreover, the history of section 1105, subdivision (a) shows that it was meant to relate to a specific, limited subject matter. Prior to the enactment of the Insurance Code the provisions as to investment of insurance companies were contained in section 421, Civil Code, the prohibition of benefits of officers etc., from such investments or of interest in the sale of assets in section 421a of the same code. Among the provisions of section 421 was the following: "It shall be the duty of the secretary of any such investing corporation to report in writing during the months of January and July of each year to the insurance commissioner the data above set forth respecting each such investment, and the insurance commissioner may, if any such investment is not approved by him, *require the corporation to sell* or dispose of the same." (Emphasis ours.) The last sentence of section 421a then contained the exception which is now section 1105 subdivision (a), Insurance Code: "Nothing contained herein, however, shall prevent the purchase by any such person of any asset which the insurance commissioner may *require to be sold*, at a price approved by him, . . . " (Emphasis ours.) There can be no doubt that the above provision of section 421a was intended to relate to the quoted provision of the preceding section. At the enactment of the Insurance Code the quoted provision of section 421 became with a few changes section 1202, Insurance

Code, and it was later recast to provide that the Commissioner may in his discretion and after hearing by written order require the disposal of any investment made in violation of the provisions of this article. In 1945 the Commissioner was also given power to demand disposal of specific investments in real estate if he decides that the interest of the insurer so requires. (Ins. Code, § 1194.9.) [5] We are of the opinion that the present provision of section 1105, subdivision (a), Insurance Code, relates to the specific provisions of sections 1202 and 1194.9 in the same manner as formerly the provision of section 421a, Civil Code, related to the one in section 421, Civil Code. [6] There is in the code no provision which gives the Commissioner power to demand the disposition of all assets of an insurer or of his whole business as a going concern. The exception of section 1105, subdivision (a), is therefore applicable only to disposition of specific assets demanded by the Commissioner on the basis of specific powers given him in the code and not to the agreement here under review.

[7] In holding that said agreement is void as violative of section 1101, subdivision (c) of the Insurance Code, we are convinced that we do not extend the application of said provision further than is necessary to effectuate its purpose, which is to prevent all possibility that those who have authority over an insurer might profit or their action might be influenced by the desire to profit from the acquisition of the assets of said insurer. The difficulties in this case were caused by the conduct of the members of the Attorney, who were simultaneously in the insurance business for their own account in corporate form and who interlaced the business of their private corporation and the business of the Exchange which they managed to such a degree that the Commissioner would not permit the resulting situation to continue. Even if their said conduct was in good faith and proper, as found by the court below, it would create a precedent wholly adverse to the purpose of section 1101, subdivision (c), if they were permitted to solve the difficulties so caused by absorbing the going business of the Exchange into their privately owned corporation, even if the price they paid for it would be adequate.

[8] Evidently if the transaction is a sale violating section 1101 and section 1106, Insurance Code, the Commissioner's approval can not override the law and validate the agreement where the code does not grant him power to do so.

As it will be our decision that the original action for declaratory relief must be dismissed and there will be no new

trial the above fully disposes of said action and none of the many points advanced by the parties in that respect require review. However the cross-actions which among other things claim for the Exchange all the business of the Company are in part not dependent on the validity of the agreement merging Exchange and Company and the correctness of the denial of all relief to cross-complainants must therefore be reviewed.

The claims of appellants to all the business of Company are governed by a principle developed mainly with respect to the relation between corporations and their directors and officers and there known as the doctrine of corporate opportunities. **[9]** Since the leading case of *Guth* v. *Loft*, 23 Del.Ch. 255 [5 A.2d 503], it has been generally accepted that a corporate officer or director may not seize for himself to the detriment of his company business opportunities in the company's line of activities which the company has an interest and prior claim to obtain, and that if he seizes them in violation of his fiduciary duty the corporation may claim for itself all benefits so obtained by him. **[10]** The doctrine was applied in this state to joint venturers in *MacIsaac* v. *Pozzo*, 81 Cal.App.2d 278 [183 P.2d 910] and is equally applicable in all situations in which a person manages or transacts business for another or for others to whom he stands in a fiduciary relation without being trustee of an express trust. **[11]** The position of the attorney-in-fact of a reciprocal insurance exchange, who manages the business of the exchange under powers of attorney of the subscribers, who provide the means for the reciprocal insurance enterprise, is fiduciary in character to the same extent as that of the management of an incorporated mutual insurance company, although neither is a real trustee. (See *Caminetti* v. *State Mut. Life Ins. Co.*, 52 Cal. App.2d 321, 323 [126 P.2d 165]) and the doctrine of corporate opportunities is equally applicable.

However this doctrine does not exclude the fiduciary from all business activity of his own in the field in which he works for others. **[12]** "Generally, it is held that the directors or officers of a corporation are not, by reason of the fiduciary relationship they bear towards the corporation and the stockholders thereof, precluded from entering into and engaging in a business enterprise independent from, though similar to, that conducted by the corporation itself, provided in doing so they act in good faith and do not interfere with the business enjoyed by the corporation. . . . The directors or officers of a going, solvent corporation cannot, however, engage in a com-

peting business to the detriment of the corporation which they represent." 13 Am.Jur. 953, Corporations, § 999. To the same effect 19 C.J.S. 160, Corporations, § 785; 3 Fletcher, Corporations (1947 rev.) 214-215, § 856; Ballantine on Corporations (1946 ed.) 203 et seq., § 79. **[13]** The latter points out (p. 205) that the basis of the doctrine must be found "in the unfairness on the particular facts of a fiduciary taking advantage of an opportunity when the interests of the corporation justly call for protection," (to the same effect Prof. Scott in 37 Cal.L.Rev. 539, 551) and continues: "This calls for the application of ethical standards of what is fair and equitable to particular sets of facts. The question is indeed often a close one whether the fiduciary duty of loyalty of directors and officers requires them to offer a particular business opportunity which they discover in connection with the corporate business to the corporation . . . or whether they may take it for themselves. This turns . . . upon various factors as to the needs and situation of the corporation, its financial ability and fair expectation under the circumstances, which cannot be reduced to definite rules." Under these circumstances the decision in each case depends on its particular facts and citation of examples is not useful. **[14]** The determination of the particular factual circumstances under which a fiduciary takes business opportunities for himself and the application of the ethical standards of fairness and good faith required from a fiduciary to said set of facts is mainly for the trier of facts. **[15]** Both the issues of good faith and of sufficient performance of contractual obligations are normally questions of fact (53 Am.Jur. p. 192, § 224; p. 231, § 273).

In this case the court below made most elaborate findings as to all circumstances on which it based its holding that the cross-defendants have not breached their fiduciary duty. Before stating their contents, we shall point out some differences between a reciprocal insurance exchange and a normal corporation which may be of importance with respect to the correctness of said holding. Stockholders in a corporation normally participate for the purpose of making profit either in the form of dividends or of increase in the value of their holding. Subscribers in an interinsurance exchange do not participate for that purpose but for the purpose only of obtaining insurance for themselves at a price and in a manner attractive to them. (There was some express testimony to that effect in this case.) Expansion of a lucrative business so

far as that is possible on the basis of the capital provided by the stockholders or accrued in prior business will as a rule benefit the stockholders, whereas subscribers of a reciprocal insurance exchange do not necessarily profit from further expansion once a sufficient size is reached to secure adequate spread of risk and stability of rate of loss; the savings and the policies that share in their distribution may well increase in the same proportion. It is clear that if it were found that further expansion would not benefit existing subscribers, that fact might be considered in deciding whether the attorney-in-fact had violated his fiduciary duty in taking opportunities for further insurance business for himself.

Another distinction to be noted is that the business of a corporation is normally transacted by means of personnel, offices and equipment built up and paid for by the company, so that the company only is entitled to their services and use and directors or officers who use any of them for their private business ventures thereby violate their fiduciary duty. In a reciprocal insurance exchange and at any rate in the exchange here involved, the attorney-in-fact contracts to provide and pay for the whole management and administration of the Exchange including all personnel, offices and equipment required for the transaction of the business of the Exchange in consideration of certain fixed percentages of the net premiums deposited, which consideration is therefore dependent on the size of the business transacted only, not on the costs of providing personnel, offices and equipment. There is therefore not necessarily a requirement that the personnel and plant which the attorney-in-fact builds up and pays in his business of insurance management be used by him for the management of the one enterprise only in relation to which he started it, if the management and administration he provides for that first enterprise remain good.

We now turn to the circumstances found by the court. From the substance of its findings we note the following; the numbers are those of the findings from which the statements preceding them were taken:

Neither before nor after the entry of the Company into business did the Exchange write nonparticipating policies, the attorney having been advised that such would violate the Insurance Code (10). Company started in workmen's compensation insurance business in 1940 by issuing nonparticipating policies to supplement the participating insurance offered by the Exchange and thus to make profit for the Com-

pany (18). The Exchange, which had until 1942 mostly sold insurance directly to the insureds, then changed its policy to sell through agents and brokers, who control 75 per cent of the workmen's compensation insurance business in California and whose reluctance to place business with a carrier who sells directly to insureds would have hampered the acquisition of additional business by Exchange (19, 20, 21). In 1943 Company began to write also participating workmen's compensation insurance to supplement the types of insurance offered with participating insurance in a stock company for which there was demand (22). The name "Industrial Indemnity" and certain insignia used by both Company and Exchange were originated by the Attorney and used by Exchange before they were used by Company; the use by Company did not cause confusion or loss of any business by Exchange (11). Since 1939 the Attorney and the Company used the same offices, equipment and personnel. Originally they were those of the Attorney, Company paying Attorney for their use a percentage of Company's net premium income. Since 1946 Company, having taken over offices, equipment and personnel of the Attorney, was paid by Attorney 14 per cent of the net premium income of Exchange out of the 17½ per cent of said income which Attorney received for its services as such. The 14 per cent constituted the actual cost to Company of the facilities and services made available to the Attorney. The Attorney retained its own function and responsibility. The contract was to the advantage of Exchange and was reasonable and proper. Company and Attorney at all times maintained separate books and records (31-34). The Attorney and Company always maintained the separate characteristics of Company and Exchange; insurance brokers, agents and insureds were always familiar with their separate entities (17). It was the policy of the Exchange to write policies of larger premium size, policy of the Company to write those of smaller premium size (28). Company paid approximately 2½ per cent more commission than Exchange to compete with other stock company insurers, Exchange returned approximately 2½ per cent more savings than Company. Insurance buyers utilized Company and Exchange according to their separate characteristics, Exchange for larger risks, Company for smaller and nonparticipating risks (36). The owners of the Attorney and Company had no interest in procuring new business for Company to the prejudice of Exchange and did not procure any business for Company to the prejudice of

Exchange, nor did they cause to be placed in Company any business that could have been placed in Exchange (102, 97). They and their agents made no attempt to attract business to the Company rather than to the Exchange and often placing of insurance in Exchange was more recommended by them than placing in Company (24). No known or appreciable business was lost by Exchange, which would have been placed in it had it not been placed with Company, and substantial business was gained by Exchange as a result of the Company's being in business (23, 25-27). Company has never been operated in competition with Exchange (23, 96, 102). Prior to 1940 Exchange had reached a size sufficient to secure adequate spread of risk and stability of loss ratio. Further acquisition of new business would not result in any advantage to its existing subscribers by reduction of premium, better service, increase of premium returned to them or in any other way. During 1948 and several prior years Exchange wrote the largest volume of premiums of all reciprocal workmen's compensation insurance carriers in California. (29, 99). The Company did not at any time in the operation of its business use any funds, facilities or information belonging to, or secured through, the Exchange (104). To engage in workmen's compensation insurance business through the medium of Company was no violation of any duty owed by the Attorney or its members to the subscribers of Exchange (98). The insurance business now being transacted, or at any time transacted, by Company is neither in law nor in equity the property of Exchange or its subscribers (100).

As we have held that the establishing of the circumstances under which the Attorney engaged in workmen's compensation insurance business of its own and the weighing of these circumstances in relation to the duty of fairness and good faith incumbent on the Attorney as a fiduciary were matters of fact, the decision of which by the trier of facts is as a rule binding on appeal, it seems evident that the findings stated are fatal to the appeal with respect to the claims of subscribers of Exchange to the business of Company unless appellants have shown that they are not supported by the evidence. This they have failed to do. In their opening briefs they have ignored them. By way of replication it is argued that the findings are based on undisputed facts substantially all presented by respondents and that although the inferences made from these facts in the findings are in dispute, such inferences drawn from undisputed testimony are no more than conclusions of

law not binding on a reviewing court. This theory is wholly erroneous, apart from the question whether it is true that there was no conflict in the evidence. This court held in *Spolter* v. *Four-Wheel Brake Serv. Co.*, 99 Cal.App.2d 690, 693 [222 P.2d 307], quoting in support *Mah See* v. *North American Acc. Ins. Co.*, 190 Cal. 421, 426 [213 P. 42, 26 A.L.R. 123], that it is settled law that if conflicting inferences may reasonably be drawn from the evidence, even if it is uncontradicted or all facts are admitted, which inference shall be drawn is a question for the trier of facts and its decision cannot be set aside by the appellate court. See, also, *Hamilton* v. *Pacific Elec. Ry. Co.*, 12 Cal.2d 598, 603 [86 P.2d 829]. **[16]** Only where there is no conflict in the evidence *and no conflicting inferences can be drawn therefrom* does the finding of the trial court amount to a conclusion of law and is the finding not binding on a reviewing court. (*Export Leaf Tobacco Co.* v. *County of Los Angeles,* 89 Cal.App.2d 909, 916 [202 P.2d 622].) The above rule where findings are based on inferences does not differ in principle from the well known rule governing findings based on direct evidence, to wit, that they are binding on the reviewing court when supported by any substantial evidence. (*Vaccarezza* v. *Sanguinetti,* 71 Cal.App.2d 687, 691 [163 P.2d 470].) **[17]** It has been repeatedly held that an appellant who contends that findings of fact are not supported by the evidence, must point out the evidence involved and show wherein it does not support said findings. (*Sutro Heights Land Co.* v. *Merced Irr. Dist.*, 211 Cal. 670, 697 et seq. [296 P. 1088]; *Metzenbaum* v. *Metzenbaum,* 96 Cal.App.2d 197, 199 [214 P.2d 603].) The latter case justifies said requirement on the ground that it facilitates the disposition of litigation before appellate courts, especially where records are voluminous, and discourages rash appeals. A rule of the same kind must for the same reasons apply when appellant contends that the findings cannot by reasonable inference be derived from the evidence. As we recently said in *Richards* v. *Plumbe,* 116 Cal.App.2d 132, 134 [253 P.2d 126]: "... the burden is on the appellant to show such a lack of substantial facts in the record that the reviewing court may say as a matter of law that there is no ground upon which the trial court could have based any reasonable inference in support of its finding, and unless this burden is met, a reversal should not be ordered." The appellants herein can certainly not be absolved from said duty where the evidence before us consists of nearly 3,000 pages of reported testimony and 145

exhibits, and the findings alone cover nearly 60 pages. Those evidentiary facts as to which the parties agree do not make it clear at first sight that the inferential findings made by the trial court cannot possibly be correct, and appellants have failed to make the specific and detailed showing required from them as stated above. It is symptomatic in that respect that even in the reply briefs only one finding is specifically mentioned, to wit, the finding that Company has never been operated in competition with Exchange. This finding evidently follows as a reasonable inference from other findings of probative facts succinctly stated by us, but wholly ignored by appellants even in their replication, although these evidentiary facts found clearly tend to destroy all elements of competition, detriment to the Exchange, and bad faith of the Attorney. Under these circumstances it is not for us to say that the ultimate findings of the court below are necessarily improper inferences nor can we hold as a matter of law, contrary to said findings, that the Attorney breached its fiduciary duty to subscribers when it engaged in the writing of workmen's compensation insurance through the medium of Company or that the business of Company was in equity the property of Exchange.* We are the more satisfied that this result is not unjust because the gain by Exchange of all profits of the business of Company without participation in them by any of Company's insureds would have given the subscribers of the Exchange a windfall wholly out of line with the setup of such Exchange.

[18] However it does not follow that cross-complainants are not entitled to any relief. Although we hold that the subscribers of Exchange are not entitled to the business built up by Company in general—and then they are necessarily not entitled either to the business of its wholly owned subsidiary, Industrial Service Company, mentioned separately on appeal —they have a right to the business taken over by Company in consequence of the transfer and assumption agreement, which we have held to be invalid. If they so desire they are entitled to have that matter wound up in these equity proceedings and for that purpose the judgment denying all relief on the cross-complaints will also have to be reversed.

Appellants do not assign as error the failure of the court below to make in the judgment express declarations of right as to other matters stated in the cross-complaints. As said

*The contention of intervener that findings 18, 39 and 85, which are somewhat connected with the matter here treated, contain inconsistencies is without merit.

before, all findings in that respect were adverse to cross-complainants. None of these findings were attacked in the opening briefs of appellants and even in the reply briefs no sufficient showing of insufficiency of the evidence to support them was made. On the same grounds and authorities as stated with respect to the findings regarding the alleged disloyal diversion of business by the Attorney the findings as to the other criticisms of the action of the Attorney must stand.

The desired decree rescinding intervener's consent to the transfer and assumption agreement and all matters relating to it have lost all materiality by our holding that said agreement is illegal. [19] An illegal contract cannot be ratified (*Fewel & Dawes, Inc.* v. *Pratt*, 17 Cal.2d 85, 91 [109 P.2d 650]). For the same reason consenting subscribers of Exchange cannot have been prejudiced by the fact that intervener was not permitted pending trial to amend its complaint so as to appear in a representative capacity for them, the right of rescission being the only point which its complaint added to the matters already before the court by the cross-complaint of certain defendants acting in representative capacity for all subscribers. [20] The allowance or rejection of the amendment offered at that time was within the discretion of the trial court. The ruling will not be disturbed on appeal as no abuse of discretion, no good reason for the delay and no necessity of the amendment in furtherance of justice is shown. (*Westwood Temple* v. *Emanuel Center*, 98 Cal. App.2d 755, 765 [221 P.2d 146] and cases there cited; *Peterson* v. *Peterson*, 74 Cal.App.2d 312, 323 [168 P.2d 474].)

Defendants in the cross-actions have in the court below taken the position that the cross-actions were barred by the statute of limitations and by laches and have cross-appealed from the trial court's rejection of said defenses. As in the cross-actions, relief will be granted only with respect to the consequences of the illegality of the transfer and assumption agreement to which said defenses do not apply, their cross-appeal has lost all materiality and will be dismissed.

Under the special circumstances of this case it seems just that each party bear its own costs on appeal.

The judgment is reversed with directions to the trial court to deny all declaratory relief to plaintiffs on the ground that the agreement as to which it is prayed for is void as contrary to law; if defendants-cross-complainants so desire, to grant them such relief as the court will deem fit to enable

them to recover in their representative capacity for subscribers the business and assets obtained by Company in consequence of the agreement herein held to be invalid, and to wind up fully all matters relating thereto; to make, if defendants-cross-complainants so desire and they have made a showing that financial advantages have been obtained by the subscribers they represent because of their services and the services of their attorneys, such orders as the court will deem fit fixing and allowing compensation for said services and providing for payment thereof out of the funds and assets recovered; the cross-appeal of defendants in the cross-actions is dismissed; the respective parties to bear their own costs.

Goodell, J., and Dooling, J., concurred.

A petition for a rehearing was denied May 29, 1953, and intervener and appellant's petition for a hearing by the Supreme Court was denied June 18, 1953.

[Civ. No. 15219. First Dist., Div. Two. Apr. 30, 1953.]

AUGUSTA DE LAGUNA SPAULDING, Appellant, v. HARRY LOVELL JONES, Individually and as Executor, etc., et al., Respondents.

[1] **Trusts—Evidence to Establish—Review.**—Oral testimony justifying a court in determining that a deed purporting to convey a fee simple was intended to be something different, such as a trust, must be clear and convincing, and where the trial court has declared the instrument to be what it purports to be, an appellant cannot expect a reversal unless the evidence is almost overwhelmingly the other way.

[2] **Witnesses—Credibility—Right to Disregard Uncontradicted Testimony.**—The most positive testimony may be rejected although the witness is not discredited by direct testimony impeaching him or contradicting his statements.

[3] **Trusts—Resulting Trusts—Absence of Consideration for Conveyance.**—The mere facts that a deed was made from father to

---

[2] Disregarding uncontradicted testimony in civil actions, note, 8 A.L.R. 796. See, also, Cal.Jur., Witnesses, § 156; Am.Jur., Witnesses § 864.

McK. Dig. References: [1] Trusts, § 342; [2] Witnesses, § 297(1); [3] Trusts, § 101; [4] Appeal and Error, § 1172.

APP.

C

[Civ. No. 16940. First Dist., Div. Two. Aug. 29, 1956.]

INDUSTRIAL INDEMNITY COMPANY et al., Respondents, v. GOLDEN STATE COMPANY, LTD., et al., Appellants.

APPEAL from a judgment of the Superior Court of the City and County of San Francisco. Albert C. Wollenberg, Judge. Judgment reversed with directions.

Action for declaratory relief, in which cross-action for restitution was filed. Judgment ordering restitution to defendants for amount less than that sought, reversed with directions.

THE COURT.—This is the second appeal in this case. It is taken by defendants on behalf of the subscribers as of December 31, 1948, of Industrial Indemnity Exchange, a reciprocal insurance exchange.

Plaintiffs Industrial Indemnity Company, et al. hereinafter called "Company," originally brought an action for declaratory relief regarding the rights of subscribers of Industrial Indemnity Exchange, hereinafter called "Exchange," under an agreement by which the business of Exchange was transferred as a whole to Company for a price to be distributed to the subscribers. Cross-actions were brought in behalf of the subscribers. It was claimed that all of the insurance business transacted by Company belonged in equity to Exchange and that this business had been disloyally diverted by Industrial Underwriters, a partnership, the attorney-in-fact of Exchange, hereinafter called "Attorney," whose partners substantially owned the stock of Company. The court on the first trial found in nearly all respects for plaintiffs and against the cross-complainants.

On appeal this court concluded (*Industrial Indem. Co.* v. *Golden State Co.*, 117 Cal.App.2d 519 [256 P.2d 677]) that the original action for declaratory relief should have been denied because the agreement to which it related was void as violating section 1101 of the Insurance Code. The respondents there contended, in an attempt to avoid the application of Insurance Code, section 1101, that the agreement was not a beneficial sale of assets to the Company as prohibited by the code but a transfer for the purpose of liquidation only. This court after reviewing the provisions of the "Transfer and Assumption Agreement" and commenting that the practical effect of the transaction was that Company acquired the whole business of Exchange as a going concern rejected this contention.

This court then reviewed the correctness of the denial of all relief to the cross-complainants. It was recognized that the attorney-in-fact in this situation was a fiduciary in relation to the subscribers and that the doctrine of corporate opportunities was applicable. It was further stated that the issues of good faith and of sufficient performance of contractual obligations are normally questions of fact. This court noted that the trial court made most elaborate findings as to all circumstances on which it based its holding that the cross-defendants did not breach their fiduciary duty. These findings were fatal to the appeal with respect to the claims of subscribers of Exchange to the business of Company since

the appellants failed to show that they were not supported by the evidence. This court said: "Under these circumstances it is not for us to say that the ultimate findings of the court below are necessarily improper inferences nor can we hold as a matter of law, contrary to said findings, that the Attorney breached its fiduciary duty to subscribers when it engaged in the writing of workmen's compensation insurance through the medium of Company or that the business of Company was in equity the property of Exchange. We are the more satisfied that this result is not unjust because the gain by Exchange of all profits of the business of Company without participation in them by any of Company's insureds would have given the subscribers of the Exchange a windfall wholly out of line with the setup of such Exchange.

"However it does not follow that cross-complainants are not entitled to any relief. Although we hold that the subscribers of Exchange are not entitled to the business built up by Company in general—and then they are necessarily not entitled either to the business of its wholly owned subsidiary, Industrial Service Company, mentioned separately on appeal—they have a right to the business taken over by Company in consequence of the transfer and assumption agreement, which we have held to be invalid. If they so desire they are entitled to have that matter wound up in these equity proceedings and for that purpose the judgment denying all relief on the cross-complaints will also have to be reversed."

This court concluded:

"The judgment is reversed with directions to the trial court to deny all declaratory relief to plaintiffs on the ground that the agreement as to which it is prayed for is void as contrary to law; if defendants-cross-complainants so desire, to grant them such relief as the court will deem fit to enable them to recover in their representative capacity for subscribers the business and assets obtained by Company in consequence of the agreement herein held to be invalid, and to wind up fully all matters relating thereto; to make, if defendants-cross-complainants so desire and they have made a showing that financial advantages have been obtained by the subscribers they represent because of their services and the services of their attorneys, such orders as the court will deem fit fixing and allowing compensation for said services and providing for payment thereof out of the funds and assets recovered; the cross-appeal of defendants in the cross-actions is dismissed; the respective parties to bear their own costs."

Following the filing of the remittitur in the superior court appellants filed their "Petition for Judgment and Decree Pursuant to the Opinion of the District Court of Appeal Herein." They asked the court to enter a decree determining the assets and the nature and value and extent of the business taken over by respondents in consequence of the transfer and assumption agreement and to award the same to themselves. They alleged that the District Court of Appeal directed that they be permitted to recover certain property in a representative capacity on behalf of all persons who were subscribers of the Industrial Indemnity Exchange on December 31, 1948; that the aforesaid property consisted of the business and assets obtained by the plaintiff, Industrial Indemnity Company, on January 1, 1949, in consequence of a transfer and assumption agreement held to be invalid; that said property was still in the possession of the said plaintiff, Industrial Indemnity Company, and its full amount and nature and extent had not been determined; that the District Court of Appeal had directed the superior court to grant appellants such relief as it deems fit to enable them to recover said property, to wind up fully all matters relating thereto, and to make such orders as it deems fit compensating appellants and their attorneys out of funds and assets recovered. An itemization of then known and discovered business and assets of Exchange for which recovery was sought followed. It was further alleged that there were other assets not yet discovered or identified which constituted the business of Exchange, and were the property and business of Exchange on December 31, 1948, and appellants sought leave to insert these items when ascertained.

Appellant Robert L. Johnson Corporation also filed a "Petition for Judgment and Decree Pursuant to Decision of the District Court of Appeal, and for Proceedings Thereunder." Appellant Johnson Corporation stated that it was bringing this petition in its own behalf, as one of the owners of Exchange, and as representative of all other similarly situated coowners. On motion of appellants (all appellants except the Johnson Corporation will be referred to simply as "appellants") this petition of appellant Johnson Corporation was stricken from the files.

Appellant Johnson Corporation later moved the superior court for certain orders relating to this matter. On motion of respondents this motion of appellant Johnson Corporation was stricken from the files.

Respondents answered appellants' petition for judgment and decree and their amendment to that petition. After a

lengthy trial the court made exhaustive findings of fact and set forth its conclusions of law. Judgment was entered to the effect that:

"1. That pursuant to the remittitur filed herein, Plaintiffs are not entitled to any declaratory relief in connection with the complaint for declaratory relief filed herein and any relief thereunder is denied on the ground that the agreement as to which it is prayed for is void as contrary to law and said complaint for declaratory relief is dismissed.

"2. That all business, property and assets of Exchange and subscribers at the Exchange obtained by Company in consequence of the Transfer and Assumption Agreement or at any time or in any manner have been returned to the Exchange and are now being held by Industrial Underwriters, the Attorney-in-Fact of Exchange, subject to the control and supervision of the Advisory Committee of the Exchange and the Insurance Commissioner of the State of California; That the Exchange is and has been since December 31, 1948, in liquidation; that the net value of the business, property and assets of Exchange is $323,300.39 and said sum includes all items of any value which are any part of the business, property or assets of the Exchange or the subscribers at the Exchange; that said sum shall be distributed, in liquidation of the Exchange, by Underwriters to those subscribers who had policies of insurance in effect with the Exchange as of December 31, 1948, on a basis whereby each of them will receive such proportion of said amount as his total earned premium on all policies of insurance placed with the Exchange since January 1, 1931 bears to the total earned premium since January 1, 1931 of all subscribers entitled to participate; that in determining the amount of the total earned premium of each such subscriber the Rules and Practices under Rule XV of the Manual of Rules, Classifications and Basic Rates published by the California Inspection Rating Bureau shall be used to determine the continuing identity of all subscribers in cases of changes in ownership or business form.

"3. That the Special Surplus Fund now being held by Industrial Underwriters shall be distributed and paid to Industrial Underwriters after full provision has been made, by reinsurance or otherwise to the satisfaction of the Insurance Commissioner of the State of California, for the liabilities of the Exchange.

"4. That the Exchange or the subscribers at the Exchange have no right, title or interest to or in any of the business, property or assets of Company.

"5. That pursuant to the terms of the remittitur filed herein and no financial advantage to the subscribers because of their services and the services of their attorneys having been realized, no compensation shall be awarded or allowed out of the $323,300.39 representing the net value of the business, property or assets of the Exchange herein provided to be distributed to the subscribers, for the services of Defendants and Cross-complainants or their attorneys.

"6. That all parties are to bear their own costs in this proceeding."

Appellants appeal from this judgment and appellant Johnson Corporation appeals from the judgment and from all intermediate orders, judgments and decrees. The subscribers of Exchange had a right to recover from respondents the business taken over by Company in consequence of the invalid transfer and assumption agreement. The remittitur from this court specifically directed the trial court, if appellants should so desire, to grant appellants "such relief as the court will deem fit to enable them to recover in their representative capacity for subscribers the business and assets obtained by Company in consequence of the agreement herein held to be invalid, and to wind up fully all matters relating thereto." The position of respondents, with which the trial court has agreed, is that the business and assets of Exchange taken over by Company in consequence of the transfer and assumption agreement consisted of the business in force on December 31, 1948, and the assets relating to this and prior business, subject to terms of certain Underwriters' Agreements to be discussed later. The value of this business was found to be $323,300.39 and this sum was awarded to appellants.

In their petition for judgment appellants stated in part:

"6) The aforesaid business and assets of the Industrial Indemnity Exchange [taken over by Company in consequence of the invalid transfer and assumption agreement] insofar as now known and discovered consist of the following items:

". . . . . .

"j) The good-will and trade name and insignia of the Industrial Indemnity Exchange and in this particular petitioners pray in the alternative for injunctive relief prohibiting the plaintiff, Industrial Indemnity Company, from the further use of the good-will and trade name and the insignia of the Industrial Indemnity Exchange, together with an award for the reasonable value of the use of said good-will and trade name and insignia by the said plaintiff and for damages for the use thereof or in the alternative for the reasonable market

value of the said good-will and trade name and insignia of the Industrial Indemnity Exchange as a going business on Dec. 31, 1948 (heretofore found by this Court not to exceed $1,574,569.23 (Finding LXXXV) in the sum of ..... $....."

However, appellants later amended their petition and in place and stead of the above paragraph 6j inserted another paragraph in which they claimed certain net earnings, the present value of certain future net earnings, and the value of the trade name and insignia of Exchange. All reference to goodwill was deleted.

This court in its prior opinion recognized that Company by reason of the invalid agreement came into possession of more than certain physical assets and business of Exchange. It was stated: "By taking over all assets, assuming all liabilities, including all outstanding policies of the Exchange and becoming directly liable thereon to the policy holders, the Company acquired the whole business of the Exchange as a going concern and would therefore benefit by the increase of its clientele." It was noted that Company was receiving an advantage not consistent with the position of a mere liquidator and that the Insurance Commissioner originally took the position in this matter that the subscribers should receive "an amount representing a reasonable going concern value of the Exchange as measured by the value to the Company of any Exchange business it might take over in the event of consolidation . . ." (The commissioner later changed his view somewhat apparently because of the identity between Attorney and Company, but this court stated that this would not change the fact that the Company acquired at least the investment and the going business.) It would seem from this that it was contemplated that appellants in a proper proceeding should be able to recover an amount to compensate them for the going concern value or the good will of Exchange which was received by Company as a result of the invalid agreement. However, relief of this sort was not sought by appellants.

It should be noted that the net worth of Exchange as of December 31, 1951, as computed in accordance with the provisions of the transfer and assumption agreement was $1,018,589.07. (At the time of the first trial this amount was estimated to be $1,894,347.07.) If the agreement had not been held invalid this amount would have been paid, and distributed to the subscribers.

The result is that if the present judgment stands the Company will have in fact everything, for which it agreed in the invalid agreement to pay considerably more than one million dollars to the subscribers and will pay for it only $323,300.39.

As noted above the appellants by amendment abandoned their claim for any recovery for the value of the good will of their business as such and instead sought a recovery of the net profits derived by the Company from insurance written, and in the future reasonably expected to be written, for insureds of the Exchange at the time that its business was illegally taken over by the Company. Appellants justify this course by pointing out that, while the value of good will as such is largely speculative and difficult of exact proof, at the time of the second trial they had the actual experience of four full years of operation by the Company after it had taken over the business of the Exchange under the illegal contract and the amount of business actually done by the Company with the former subscribers of the Exchange, from which the net profits accruing to the Company from such business might be calculated by deducting from the total premiums so received by the Company a proper proportion of the Company's expenses of operation.

Respondents counter with the fact that they produced evidence, which the trial court in the findings accepted, negativing any right to such recovery. This evidence may be summarized as follows: that it is the custom in the insurance business when an insurance company is purchased to value only current business and assets, no allowance being made for any going concern or good will value; that there is no such good will value because the insurance brokers review the situation annually and place their clients' insurance in whatever company, considering all relevant factors, seems most desirable and advantageous for their clients for the ensuing policy year; there was testimony of many of the largest former subscribers, aggregating approximately one-half the business done by the Company with former subscribers of the Exchange, that they placed their business with the Company, not because the Company had acquired the business of the Exchange, but solely because they were stockholders in the Company; as to the other former subscribers of the Exchange who placed their insurance with the Company there was testimony that their brokers would not advise their clients to place their insurance with the Company because it had acquired the business of the Exchange but would canvass the field and recommend the placing of such insurance with whatever company seemed

most desirable for the clients uninfluenced by the fact that the Company had acquired the business of the Exchange; and furthermore that the Exchange had in any event decided to discontinue its business. From this it is argued that the finding that the Exchange suffered no loss and hence is not entitled to any of the profit from such business is amply supported.

[1a] In assaying the validity of this position it is relevant to consider the factual situation. The sale of the business to the Company was held by us on the former appeal to be in contravention of section 1101 of the Insurance Code because of the fiduciary relation existing between the parties. Even though the Company was acting in actual good faith and in ignorance of the illegal nature of the contract it nonetheless breached its fiduciary relation in attempting to acquire the business of the Exchange in violation of the express prohibition of the law. By its breach of the fiduciary relation, and violation of an express statute enacted for the protection of the Exchange in just such a situation, it could not divest itself of its character as a fiduciary toward the Exchange. It remained in the position of a fiduciary of the Exchange after the making of the illegal contract as before. It is unthinkable that a fiduciary by a breach of its trust could terminate its fiduciary relation or find itself in a more advantageous position than it was before because of such breach.

We are thus faced with the question: Can the Company retain the profits which it secured from the former subscribers of the Exchange following its wrongful acquisition of the business of the Exchange in breach of its fiduciary duties and in violation of a statute designed to prevent it from doing just what it in fact did? Courts of equity have traditionally been concerned as much with preventing fiduciaries from benefiting from breaches of their trust as they have been with protecting beneficiaries from losses which they otherwise would not have sustained. (Cases cited *infra.*)

It must never be forgotten in considering the remedies to be afforded beneficiaries for breaches of trust by their fiduciaries that courts look with a particularly jealous eye upon the trust relation and hold fiduciaries to the highest standard of good faith. In a case often since quoted Mr. Justice Cardozo used these words: "Many forms of conduct permissible in a workaday world for those acting at arm's length, are forbidden to those bound by fiduciary ties. A trustee is held to something stricter than the morals of the market place. Not honesty alone, but the punctilio of an honor the most

sensitive, is then the standard of behavior. As to this there has developed a tradition that is unbending and inveterate. Uncompromising rigidity has been the attitude of courts of equity when petitioned to undermine the rule of undivided loyalty by the 'disintegrating erosion' of particular exceptions. (Citation.) Only thus has the level of conduct for fiduciaries been kept at a level higher than that trodden by the crowd." (*Meinhard* v. *Salmon*, 249 N.Y. 458 [164 N.E. 545, 546, 62 A.L.R. 1].)

The pertinent and controlling facts are simple and may be simply stated. By breach of its trust and in violation of the law the Company illegally acquired the business of the Exchange. It retained its fiduciary character after the illegal acquisition as before. Following this illegal acquisition it acquired and benefited from a large portion of the insurance business formerly done by the Exchange. Under these circumstances it cannot lie in the mouth of the Company to say, "The Exchange lost nothing because it would not have had the business anyway. We gained nothing which we would not have gotten in any event and so we cannot be held liable." The fact remains that the Company illegally acquired the business of the Exchange. It kept and still has many of Exchange's customers. It put itself in the position to acquire those customers by its own breach of trust and violation of the law. To permit it to profit from those customers would permit it to reap a gain from its own breach of duty and illegal act. That it might have gotten these customers in another way if it had not breached its trust and violated the law does not undo the fact that it did breach its trust and violate the law and acquire them in that way. The Company illegally scrambled the eggs. Neither it nor the courts can unscramble them now, nor place Exchange in the position in which it was before. The Company must take the consequences of what can not be undone. It cannot ask us to place it in the position in which it might have been if it had not illegally acquired and liquidated the business of the Exchange.

The Supreme Court of the United States said in *Crites, Inc.* v. *Prudential Ins. Co. of America*, 322 U.S. 408, 417 [64 S.Ct. 1075, 88 L.Ed. 1356]: "In this type of situation 'the incidence of a particular conflict of interest can seldom be measured with any degree of certainty'. (Citation.) Proof of profits resulting from an irregular or conflicting course of conduct is sufficient."

So Mr. Justice Cardozo said in *Meinhard* v. *Salmon, supra*, 164 N.E. at page 547:

"The trouble about his conduct is that he excluded his coadventurer from any chance to compete . . .

"No answer is it to say that the chance would have been of little value even if seasonably offered. Such a calculus of probability is beyond the science of the chancery."

Herein follow two equally pertinent statements of the United States Supreme Court:

"It makes no difference that the estate was not a loser in the transaction . . . It is the relation of the trustee to the estate which prevents his dealing in such a way as to make a personal profit for himself." (*Magruder* v. *Drury,* 235 U.S. 106, 120 [35 S.Ct. 77, 59 L.Ed. 151].)

"The course taken was one which a fiduciary could not legally pursue. (Citation.) Since he did pursue it and profits resulted the law made him accountable for all the profits obtained by him and those who were associated with him in the matter, although the estate may not have been injured thereby." (*Jackson* v. *Smith,* 254 U.S. 586, 588-589 [41 S.Ct. 200, 65 L.Ed. 418].)

In *Menefee* v. *Oxnam,* 42 Cal.App. 81, 87-88 [183 P. 379], the court used equally pertinent language: "Though it is the general rule that fraud without at least some slight injury is not ground for relief, this general rule is not an obstacle to recovery in cases of the kind here under consideration even though there be a total absence of injury to the complaining party . . . The rule that a coadventurer must act with utmost good faith, . . . is not intended to be remedial of actual wrong, but preventive of the possibility of it; and it matters not that there is no fraud meditated and no injury done."

In Comment (d) to section 160, Restatement of Restitution, after pointing out that while ordinarily restitution is used to restore to a plaintiff property of which he has been unjustly deprived, the text continues (pp. 643-644): "There are some situations, however, in which a constructive trust is imposed in favor of a plaintiff who has not suffered a loss as great as the benefit received by the defendant. In these situations the defendant is compelled to surrender the benefit on the ground that he would be unjustly enriched if he were permitted to retain it, even though that enrichment is not at the expense of the plaintiff. Thus, if the defendant has made a profit through the violation of a duty to the plaintiff to whom he is in a fiduciary relation, he can be compelled to surrender the profit to the plaintiff, although the profit was not made at the expense of the plaintiff."

To make the nice calculations by hindsight which respondents ask us to make in this case would reward their violation of the law by a windfall of thousands of dollars which they would have been bound to pay if their conduct had been legal. Equity should not countenance such a result if by following established equitable principles it can be avoided. One of the recognized forms of relief is the recovery of the profits accruing to the fiduciary who breaches his trust. (Rest., Trusts, § 205(b); 2 Scott on Trusts, § 170.25, p. 909, § 205, p. 1098, § 206, pp. 1105-1106, § 462.2, p. 2318.) There is nothing in our former opinion preventing appellants from recovering these profits. We intended in that opinion no more than to direct that appellants be allowed whatever recovery they might be entitled to in equity for the wrongful taking over of the business of the Exchange. We did not consider, much less decide, the extent and nature of that relief.

Respondents argue that section 1103 of the Insurance Code fixes the measure of recovery for a violation of section 1101 and that the recovery of these profits cannot be brought within its terms. Section 1103 provides: "Whenever an insurer is injured or is made to suffer loss by reason of any violation of section(s) 1101 . . . such insurer may recover . . . damages sufficient to compensate such insurer for such loss."

The section deals only with damages. The profits in question are recoverable not as damages but by way of restitution, and as we have seen without regard to loss suffered by the beneficiary. The rule was clearly stated by the court in *Speed* v. *Transamerica Corp.*, 135 F.Supp. 176, 187, quoting from Prosser on Torts: "When restitution is sought either in equity or at law a much more liberal policy has been adopted. Since the purpose is not to compensate the plaintiff's loss but to restore what the defendant has received, the courts look to the inequity of allowing him to retain it rather than to the damage which the plaintiff has sustained."

Nor can section 2238, Civil Code, avail respondents. That section reads: "A trustee who uses or disposes of the trust property in any manner not authorized by the trust, but in good faith, and with intent to serve the interests of the beneficiary, is liable only to make good whatever is lost to the beneficiary by his error." Here respondents' good faith may not be questioned but they nevertheless violated an express statute enacted for the protection of the Exchange. **[2]** Ignorance of the law is traditionally no excuse for its violation. It is sufficient that the violator intentionally does the act which

the law prohibits. (*People* v. *Dillon*, 199 Cal. 1, 7-9 [248 P. 230].)

[1b] It follows that respondents were guilty of something more than the use and disposition of trust property in a "manner not authorized by the trust" which is dealt with in section 2238, Civil Code. They dealt with the trust property in violation of an express statute in a manner forbidden by the law and made a crime by section 1106, Insurance Code. Under the circumstances of this case section 2238, Civil Code, is inapplicable. To apply it would permit respondents to reap a benefit from their own violation of the law.

We give no consideration on this appeal to the proper calculation of such net profits other than to say that the expenses of the Company properly allocable to these policies should be deducted from the premiums to ascertain such profits. The court made no finding of the amount of such net profits in the judgment appealed from. On another trial it will make such finding based on its weighing of the evidence that may be produced on the subject at that trial.

[3] A consideration of the fact that the recovery from a fiduciary of profits made from his breach of duty to his beneficiary is allowed by way of restitution without regard to the beneficiary's loss demonstrates that there can be no recovery for anticipated future profits in the circumstances of this case. It is the profits actually accruing to the fiduciary from his breach which are the subject of restitution. Respondents cannot be made to restore what they have not received. To allow an amount for anticipated future profits would be to allow damages not restitution, and damages are based on loss or injury to the plaintiff. Since in this case the court has found on substantial evidence that Exchange suffered no loss of profits there can be no award for such future loss by way of damages, as obviously there can be none by way of restitution.

Appellants suggest that the trial court in its judgment might reserve the right by supplemental judgments to award such future profits as they actually accrue. We have no doubt of the power of a court of equity to do this in the exercise of its sound discretion. Whether if the court refuses to do this such profits as they accrue may be made the basis of future action by appellants is something which has not been briefed by the parties and which we should not decide on this appeal.

In the Underwriters' Agreement there was a provision for the accumulation of a fund to go to the attorney-in-fact in

case of liquidation of the Exchange to cover costs of liquidation and compensation to the attorney-in-fact for his services as liquidator. This amounts to $592,322.21. His rights to this amount have been assigned by the attorney-in-fact to the Company. Following the first decision of this court holding the sale of the business of Exchange illegal the Insurance Commissioner licensed the attorney-in-fact to continue the liquidation of the Exchange. The trial court found that the Exchange had been liquidated in accordance with the Underwriters' Agreement and that this fund was the property of the Company under the assignment to it by the attorney-in-fact. The parties argue the question whether the void Assumption Agreement terminated the Underwriters' Agreement, appellants claiming that it did (citing *Penn. Water etc. Co.* v. *Consolidated Gas etc. Co.*, 186 F.2d 934; and *Virginia Dare Transp. Co.* v. *Norfolk Southern Bus Corp.*, 176 F.2d 354) and respondents arguing that it did not (citing 17 C.J.S.sec. 287, p. 674; *Indiana Flooring Co.* v. *Grand Rapids Trust Co.*, 20 F.2d 63; *Carson* v. *Sinking Fund Com.*, 2 Lyc. 3 (Pa. Com. P.); and *Tearney* v. *Marmiom*, 103 W.Va. 394 [137 S.E. 543].) This question seems somewhat beside the point. The undisputed and indisputable fact is that neither the attorney-in-fact nor the Company acted or purported to act under the Underwriters' Agreement in liquidating the Exchange. The liquidation of the Exchange was accomplished in violation of law and of the rights of the subscribers of the Exchange by the Company acting under the illegal Assumption Agreement and as owners of the business of the Exchange. What respondents are in effect saying is: "True we acted under an illegal agreement in liquidating the Exchange as its owners. But now that the court has held the agreement illegal and that we are not the owners of the business, it is proper for the court to treat our illegal conduct as if it had been legal and put us in the same position after the fact of our illegal conduct as we would have been if we had not proceeded to liquidate the business illegally but instead had liquidated the business legally under the Underwriters' Agreement." **[4]** Equity should not reward the wrong-doer by giving him rights under a contract which he himself illegally breached and repudiated. It is a settled principle of equity that no one can profit from his own wrong. (Civ. Code, § 3517.)

[5] If a court could have acted promptly enough to set aside the illegal Assumption Agreement before the illegal liquidation had proceeded to the point of no return it is possible that the attorney-in-fact might have then proceeded

with the liquidation under the terms of the Underwriters' Agreement, but by the time this court had held the Assumption Agreement illegal in 1953, the illegal liquidation had proceeded to a point where the parties could not be put *in statu quo* by the restoration of the going business to them. Equity was compelled to give them restitution in value not in kind and to allow the liquidation theretofore carried on in violation of express law to proceed to its conclusion. That is not to say that what has been done illegally was thereby rendered legal. The liquidation under the illegal assumption agreement was and remains illegal and it is that illegality that is at the heart of this action. *Ex post facto* the courts cannot legalize that illegal action nor treat it as if it had been legal by now attributing it to another agreement under which, but for the illegal Assumption Agreement, it might have been legally taken.

However, we are satisfied that in striking the balance between the parties the actual costs reasonably incurred by respondents in liquidating the business should be allowed to them. Appellants are entitled to the reasonable value of the business and assets illegally taken over by the Company, but any reasonably necessary charges connected with those assets are properly deductible therefrom. All reasonable expenses necessarily involved in discharging the obligations of the Exchange are properly deductible in determining the net value of the assets taken over.

What we have said necessarily disposes of the claim to an amount of compensation provided in the Underwriters' Agreement to be paid to the attorney-in-fact as compensation for his services calculated on a percentage of the premiums actually received by the Exchange. When the business was taken over illegally by the Company the policy years on many of the policies written by Exchange had not expired and it was impossible to determine the exact amount of the premiums on which the compensation of the attorney-in-fact should be based. The attorney-in-fact assigned his rights to these fees to the Company and the trial court found that the Company was entitled to them. Appellants attack this finding on the ground that the Underwriters' Agreement under which they were payable was terminated by the illegal Assumption Agreement.

Respondents argue that since they took over the business in January 1, 1949, and continued the services formerly performed by the attorney-in-fact, the entire fee was earned by the services of the attorney-in-fact performed up to that date

and the services performed by the Company after that date. Both parties seem to us somewhat to miss the mark. In our judgment respondents should be compensated for the portion of the services actually performed by the attorney-in-fact under the Underwriters' Agreement up to the date of the take-over by the Company. But the Company was not acting as attorney-in-fact under the Underwriters' Agreement after January 1, 1949, in reinsuring these existing policies of the Exchange and running out their terms. Respondents admit this fact in their brief on page 49 when they say: "Since the company was handling this business after January 1, 1949 for its own account, it obviously did not draw a separate check to its own order out of its own funds in payment of this fee." Since "the Company was handling this business after January 1, 1949 *for its own account*" it just as obviously was not handling it as attorney-in-fact under the Underwriters' Agreement on the Exchange's account. Here again respondents are asking us to treat as legally done under the Underwriters' Agreement what in fact was illegally done under the Assumption Agreement. The proper allocation of fees to the attorney-in-fact should take into account the services actually performed by the attorney-in-fact for the portion of the policy years that he acted as attorney-in-fact as related to the services performed by the Company for the balance of the respective policy years. Respondents should be credited only with the portion of the contractual fees properly allocable to the services actually performed by the attorney-in-fact as related to the total services that he would have performed in connection with the various policies if his services had continued under the Underwriters' Agreement until the end of the policy years.

[6] We regard this allocation as equitable for the following reasons: The attorney-in-fact in good faith performed the services, for which he was to be compensated, up to the effective date of the take-over. Thereafter he ceased to perform those services only because he believed in good faith that the Assumption Agreement was legal and valid and superseded the Underwriters' Agreement. In doing equity between the parties the attorney-in-fact should be paid for the services actually performed in good faith by him pursuant to the Underwriters' agreement, but no compensation should be allowed for the illegal conduct of respondents after the effective date of the take-over. The contract furnishes the measure of compensation spread over the entire life of each policy. That measure can only be effectively applied under

the facts of this case by an allocation of a portion of the compensation equal to the portion of the services performed by the attorney-in-fact while he was acting under the Underwriters' Agreement.

[7] The trial court allowed no interest on its award. In this connection it seems important that respondents were not acting in bad faith but under the mistaken belief, bolstered by the approval of the Insurance Commissioner, that the assumption agreement was a valid and legal one.

In *Title Ins. & Trust Co.* v. *Ingersoll*, 158 Cal. 474, 489 [111 P. 360] (a trust case) we read:

"The question whether any interest should be charged, and if any, how much, depends on the circumstances of the particular case, and they may be such that a mere restoration of the property, or its value, without any interest, would be all that justice would require. (*Wheeler* v. *Bolton*, 92 Cal. [159] 172 [28 P. 558].)"

So this court recently held that in equity the awarding or refusal to award interest on unliquidated amounts is discretionary with the court. (*Leonard* v. *Huston*, 122 Cal.App. 2d 541 [265 P.2d 566].)

That the courts generally agree that the charging or withholding of interest in such cases lies in the sound discretion of a court of equity see 90 Corpus Juris Secundum, Trusts, section 338, page 584 and cases cited in notes 60 and 61.

It must be borne in mind that more than four years elapsed between the effective date of the Assumption Agreement and the decision of this court in 117 Cal.App.2d 519 [256 P.2d 677]. During that entire period no question was ever suggested of the illegality of the Assumption Agreement. This court was the first to raise the question on its own initiative. The charging of interest for this period would penalize respondents for their good faith action in ignorance of a law of which appellants were equally ignorant. Following this the case required, and will on another trial require, a long and complicated accounting. Under the circumstances we believe that the following language from *Stockton Theatres, Inc.* v. *Palermo*, 121 Cal.App.2d 616, 632 [241 P.2d 54] is particularly applicable:

"Whether, therefore, it would be just and equitable that interest be charged from the date the remittiturs were returned upon such sum as after a long and complicated accounting might have been found then to have been due presented a question calling for judicial discretion in determining what equity required. This, therefore, we think

presented an issue peculiarly for the trial court to determine insofar as the allowance of interest upon the amount ultimately found due be concerned, and we cannot say on this record that the trial court abused that discretion or in the refusal to allow interest prior to judgment failed to do equity. Generally speaking, where an accounting is required in order to arrive at a sum justly due, interest is not allowed. (Citing cases.)"

Upon another trial the question of allowing interest or not, upon the whole or any part of the judgment, and if allowed, from what date or dates it should run on any amount or amounts, will be again a matter upon which the trial court may exercise its sound discretion. It is clear from the authorities cited on this point that the code sections on interest cited by appellants are not binding upon a court of equity in this type of case.

Appellant Johnson argues that the trial court erred in allowing Company to absorb Exchange and in not decreeing the restoration of the business of Exchange as a going concern. Nobody can uneat an apple. Exchange had ceased to be a going concern years before the second trial and Company had in fact absorbed it. The course pursued by the other appellants was the only realistic one left to pursue because the only thing that the court could effectively decree was a restoration in terms of money of the value of a business that was gone beyond the recall of any decree of court. Appellant Johnson does not offer any workable suggestion by which the impossibility of restoring what no longer exists could be accomplished.

This appellant further argues that the name and insignia of Exchange should have been restored to it and the Company enjoined from using them. One answer is that there is no longer an Exchange to which anything could be restored. The Exchange is gone beyond recall. This action on the cross-complaint is one in a representative capacity on behalf of former subscribers of the Exchange. A second answer is that on another trial cross-complainants will get restitution of the value of the business of Exchange, together with all of its assets in an amount to be determined after an accounting pursuant to the directions of this court, plus the net profits accruing to Company from its illegal taking over of the business. The name and insignia are a part of the business so taken over and if of any value, which respondents dispute, are a part of the business and assets compensated for in this fashion.

Finally, appellant Johnson asks us to order that it represent all subscribers on another trial on the ground that the other appellants have demonstrated that they are not properly representing them. As we said above, the other appellants have taken the only realistic approach to the case and we find no good reason to supersede them. The court did not err in dismissing appellant Johnson's cross-complaint. **[8]** In a representative action, such as this, the court is not bound to permit the intervention of others of the class if their interests are being properly protected. (*Mann* v. *Superior Court*, 53 Cal.App.2d 272, 280-281 [127 P.2d 970].)

The judgment is reversed with directions to the trial court to retry the case and award judgment in accordance with the principles herein expressed. Appellant Johnson to bear its own costs of appeal. The other appellants to recover their costs of appeal from respondents.

LIBRARY
SUPREME COURT, U. S.

FILED
MAR 26 1958
JOHN T. FEY, Clerk

IN THE

Supreme Court of the United States

October Term, 1957.

No. 801

G. W. THOMAS DRAYAGE & RIGGING COMPANY, INC., a corporation, W. R. BALLINGER & SON, a corporation, and MINNA M. BALLINGER,

Petitioners,

vs.

INDUSTRIAL INDEMNITY COMPANY, a corporation; INDUSTRIAL INDEMNITY EXCHANGE, a reciprocal exchange; T. G. McGUIRE, E. A. MATHIESSEN, S. E. HODAPP, J. V. CHAMBERS, M. S. FIELDS, E. E. URSIN, D. W. SCHIEBEL, W. A. HALUK, R. E. MAY, JR., R. L. JONES, JR., FRED DREXLER, N. S. YOUNG, THOMAS SOULE, J. P. TAHENY and V. E. HOWARD, JR., doing business as Industrial Service Company, a copartnership, HENRY J. KAISER, K. K. BECHTEL, S. D. BECHTEL, JOHN A. McCONE, W. A. BECHTEL, JR., T. G. McGUIRE, E. S. DULIN, F. SOMERS PETERSON, JAMES M. SMITH, M. I. SMITH, ALDEN G. ROACH, ROBERT L. BRIDGES, H. S. LORD, A. F. BISHOP, all of the aforesaid doing business as INDUSTRIAL UNDERWRITERS, a partnership, K. K. BECHTEL, L. T. KETT, F. SOMERS PETERSON, J. W. SCAMMELL, G. G. SHERWOOD, EMERSON SPEAR, A. G. STREBLOW, G. J. THOMPSON, W. E. WASTE, JOSHUA HENDY IRON WORKS, a corporation, INTERNATIONAL ENGINEERING COMPANY, INC., a corporation, and MARINE TERMINALS CORPORATION, a corporation,

Respondents.

On Petition for a Writ of Certiorari to the Supreme Court of the State of California.

REPLY BRIEF FOR PETITIONERS.

ROBERT W. KENNY,
1557 Beverly Boulevard,
Los Angeles 26, California,
FRANK B. BELCHER,
Attorneys for Petitioners.

BELCHER, KEARNEY & FARGO,
KENNY & MORRIS,
JEROME POLITZER,
MORRIS E. COHN,
HYMAN & HYMAN,
Of Counsel.

Parker & Son, Inc., Law Printers, Los Angeles. Phone MA. 6-9171.

SUBJECT INDEX

PAGE

I.

The federal questions were properly raised, were necessary to a determination of the case, and no adequate non-federal ground of decision is presented by respondents 1

II.

The court below arbitrarily deprived petitioners of their property contrary to fundamental principles of justice and due process of law embodied in the Fourteenth Amendment to the Constitution of the United States 4

III.

A substantial federal question is presented when it is claimed that a state court arbitrarily and capriciously and contrary to inherit principles of justice has taken the property of one person and given it to another without compensation in violation of the due process and equal protection provisions of the Fourteenth Amendment 6

Conclusion 7

TABLE OF AUTHORITIES CITED

CASES PAGE

Missouri v. Gehner, 281 U. S. 313 4

Oyama v. California, 332 U. S. 633 6

Rice v. Sioux City Cemetery, 349 U. S. 70 5

IN THE

Supreme Court of the United States

October Term, 1957.

No. 801

G. W. THOMAS DRAYAGE & RIGGING COMPANY, INC., a corporation, W. R. BALLINGER & SON, a corporation, and MINNA M. BALLINGER,

Petitioners,

vs.

INDUSTRIAL INDEMNITY COMPANY, a corporation; INDUSTRIAL INDEMNITY EXCHANGE, a reciprocal exchange; T. G. McGUIRE, E. A. MATHIESSEN, S. E. HODAPP, I. V. CHAMBERS, M. S. FIELDS, E. E. URSIN, D. W. SCHIEBEL, W. A. HALUK, R. E. MAY, JR., R. L. JONES, JR., FRED DREXLER, N. S. YOUNG, THOMAS SOULE, J. P. TAHENY and V. E. HOWARD, JR., doing business as Industrial Service Company, a copartnership, HENRY J. KAISER, K. K. BECHTEL, S. D. BECHTEL, JOHN A. McCONE, W. A. BECHTEL, JR., T. G. McGUIRE, E. S. DULIN, F. SOMERS PETERSON, JAMES M. SMITH, M. I. SMITH, ALDEN G. ROACH, ROBERT L. BRIDGES, H. S. LORD, A. F. BISHOP, all of the aforesaid doing business as INDUSTRIAL UNDERWRITERS, a partnership, K. K. BECHTEL, L. T. KETT, F. SOMERS PETERSON, J. W. SCAMMELL, G. G. SHERWOOD, EMERSON SPEAR, A. G. STREBLOW, G. J. THOMPSON, W. E. WASTE, JOSHUA HENDY IRON WORKS, a corporation, INTERNATIONAL ENGINEERING COMPANY, INC., a corporation, and MARINE TERMINALS CORPORATION, a corporation,

Respondents.

On Petition for a Writ of Certiorari to the Supreme Court of the State of California.

REPLY BRIEF FOR PETITIONERS.

I.

The Federal Questions Were Properly Raised, Were Necessary to a Determination of the Case, and No Adequate Non-Federal Ground of Decision Is Presented by Respondents.

Respondents are fruitlessly attempting to avoid any analysis of the second opinion of the District Court of Appeal (App. C; 144 A. C. A. 244, 301 P. 2d 112) which

reversed the judgment of the Superior Court and held that petitioners had had been unlawfully and arbitrarily deprived of their property privileges and interests (Pet. pp. 13-14). Of course, the judgment of the Supreme Court replaced the judgment of the District Court of Appeal, and it was a review of that judgment which is sought in this Court. But on the question of jurisdiction, the issue is not the effectiveness of the different judgments of the various courts, but whether the decision of the Supreme Court, in the light of all prior proceedings, was one which could not reasonably be anticipated (Pet. pp. 32-35).

In this connection, respondents do not dispute that the District Court of Appeal initially held that the unlawful transfer of Exchange by its unfaithful fiduciary was not a liquidation of Exchange, but a sale of a going business (Pet. pp. 9-10, 28-29); that "Company acquired the whole business of the Exchange as a going concern and would therefore benefit by the increase of its clientele" (App B, p. 529). Nor is it disputed that the District Court of Appeal thus held that the subscribers of Exchange "have a right to the business taken over by Company in consequence of the transfer and assumption agreement" (App. B, p. 539).

Nor do respondents dispute that they filed no petition for hearing from this first decision of the District Court of Appeal, that the issues were raised on a petition by an intervening party and that the petition for hearing was denied by the Supreme Court (Pet. p. 10). Respondents

argue that if the legal principles thus enumerated by the courts of California became settled (see Pet. p. 33), still the courts had the *power* to disregard them (Resp. Br. p. 12, fn. 9). But the question is not one of power, but whether petitioners had any reason to anticipate that the court below would arbitrarily exercise such alleged power in the case herein. Respondents have not met this issue (see Pet. pp. 21-30).

When the law of the case thus established was so plainly disregarded by the Superior Court, petitioners in accordance with the law of California (Pet. p. 33) properly sought redress from the same Appellate Court which had established the governing law. *That court sustained the position of petitioners on all respects* (Pet. pp. 13-14). The District Court of Appeal reviewed its prior decision (App. C, pp. 246-247), the subsequent proceedings (App. C, pp. 248-251), and held again that Exchange, in violation of law, had been sold as a going business and not for purposes of liquidation, that the subscribers were entitled to the net worth of the assets of Exchange including the investment earnings and the net profits resulting from the business of Exchange unlawfully obtained by Company (App. C, pp. 251-263).

It thus appears plain why respondents seek to avoid discussion of the decision and judgment of the District Court of Appeal on the case herein. At that point petitioners had been completely vindicated; respondents had been decisively condemned for their unlawful conduct. It was the decision of the court below, sharply divided, which

for the first time effectively gave respondents an uneffected windfall of over $5,000,000.00. That decision, for all the stated reasons, was a complete surprise and completely unexpected, and one which could not be reasonably anticipated (Pet. pp. 14-17, 21-30).

> "Upon the facts disclosed by this record it is clear that appellant sufficiently raised in the highest court of the State the federal questions here presented and is entitled to have them considered."
>
> *Missouri v. Gehner,* 281 U. S. 313, 320.

II.

The Court Below Arbitrarily Deprived Petitioners of Their Property Contrary to Fundamental Principles of Justice and Due Process of Law Embodied in the Fourteenth Amendment to the Constitution of the United States.

The respondents seek to support the judgment on the basis of "state law". They repeat the "findings" of the trial court, urge that the findings were supported by the evidence, and that the majority decision of the court below should therefore be undisturbed. It is significant that respondents also state that

> "irrespective of this legal result, K. K. Bechtel, the president of Company, affirmed its intention to see that the subscribers in fact received whatever would have come to them under the technically illegal agreement, less costs of litigation." (Resp. Br. p. 7, fn. 7.)

In short, respondents express willingness to pay the subscribers the stipulated sum of $1,018,539.07 although the only legally enforceable judgment against them is now in

the sum of $323,300.39. In assessing the arbitrary nature of the judgment of the court below, this significant concession of the malefactor, and its implications, should not be overlooked.

Respondents have made not the slightest attempt to dispute the petitioners' arguments that the holding of the court below was essentially arbitrary and capricious, unsupported by the evidence, and flowing solely from a failure to apply settled principles of justice and common law usages to undisputed facts. Respondents cannot dispute that Attorney and Company had the same stock ownership (App. A, p. 260); that the transfer of Exchange by Attorney to Company was not only in violation of express law, but in violation of fiduciary principles essential in an ordered society;* and that Company illegally obtained the business and assets of Exchange (Pet. p. 21).

Respondents have refrained from discussing the essential basis of the decision below denying the subscribers of Exchange the profits unlawfully appropriated by Company (Pet. pp. 23-27); the arbitrary nature of the ruling denying Exchange its investment earnings (Pet. pp. 27-29); and the wholly baseless ruling charging subscribers of Exchange for services rendered by Company to its own clients (Pet. pp. 29-30). Respondents would deny this Court's jurisdiction to review solely on the basis of the

---

*Such violations by fiduciaries of insurance exchanges can always arise again and have an adverse effect on the public or other litigants. Respondents cannot, therefore, properly rely on *Rice v. Sioux City Cemetery*, 349 U. S. 70 (Resp. Br. pp. 5, 17), which is inapposite.

"findings", without proving that the findings are supported by the evidence and without showing that these findings are not intermingled with the federal questions here involved (see Pet. pp. 21-32, 34). Such failure of proof, in the light of the claims made by petitioners and their analysis of the record and legal issues in the petition for a writ of certiorari herein, renders the opposition of respondents to this Court's jurisdiction ineffectual, it is respectfully submitted.

> "In approaching cases, such as this one, in which federal constitutional rights are asserted, it is incumbent on us to inquire not merely whether those rights have been denied in express terms, but also whether they have been denied in substance and effect. We must review independently both the legal issues and those factual matters with which they are commingled."
>
> *Oyama v. California,* 332 U. S. 633, 636.

III.

A Substantial Federal Question Is Presented When It Is Claimed That a State Court Arbitrarily and Capriciously and Contrary to Inherit Principles of Justice Has Taken the Property of One Person and Given It to Another Without Compensation in Violation of the Due Process and Equal Protection Provisions of the Fourteenth Amendment.

Respondents, in disregard of the record and the claims of petitioners, have attempted to relegate the issue here to the question whether a judgment determining the ownership of property, after trial is reviewable by this Court for miscellaneous errors in law or in fact. (Resp. Br. pp.

16-18.) That is not the issue here. The question involved here is whether the judgment of the court below did not operate *to arbitrarily and capriciously* take the private property of Exchange and its subscribers, without their consent, for the private use and benefit of respondents, in violation of the pertinent provisions of the Fourteenth Amendment. Respondents have refrained from meeting those claims on the facts (Pet. pp. 19-32), and they have not disputed the applicable law sustaining this Court's jurisdiction when the conclusions of arbitrariness and injustice are sustained. (Pet. pp. 18-19, 30-32.)

Conclusion.

The petition for a writ of certiorari should be granted.

Respectfully submitted,

ROBERT W. KENNY,
FRANK B. BELCHER,
Attorneys for Petitioners.

BELCHER, KEARNEY & FARGO,
KENNY & MORRIS,
JEROME POLITZER,
MORRIS E. COHN,
HYMAN & HYMAN,
Of Counsel.

SUPREME COURT, U. S.

Office - Supreme Court, U.S.
FILED
MAR 22 1958
JOHN T. FEY, Clerk

In the Supreme Court of the United States

OCTOBER TERM, 1957

No. 801

G. W. THOMAS DRAYAGE & RIGGING COMPANY, INC., a corporation, W. R. BALLINGER & SON, a corporation, and MINNA M. BALLINGER,
Petitioners,

vs.

INDUSTRIAL INDEMNITY COMPANY, a corporation; INDUSTRIAL INDEMNITY EXCHANGE, a reciprocal exchange; T. G. McGUIRE, E. A. MATHIESSEN, S. E. HODAPP, J. V. CHAMBERS, M. S. FIELDS, E. E. URSIN, D. W. SCHIEBEL, W. A. HALUK, R. E. MAY, JR., R. L. JONES, JR., FRED DREXLER, N. S. YOUNG, THOMAS SOULE, J. P. TAHENY and V. E. HOWARD, JR., doing business as Industrial Service Company, a copartnership, HENRY J. KAISER, K. K. BECHTEL, S. D. BECHTEL, JOHN A. McCONE, W. A. BECHTEL, JR., T. G. McGUIRE, E. S. DULIN, F. SOMERS PETERSON, JAMES M. SMITH, M. I. SMITH, ALDEN G. ROACH, ROBERT L. BRIDGES, H. S. LORD, A. F. BISHOP, all of the aforesaid doing business as INDUSTRIAL UNDERWRITERS, a partnership, K. K. BECHTEL, L. T. KETT, F. SOMERS PETERSON, J. W. SCAMMELL, G. G. SHERWOOD, EMERSON SPEAR, A. G. STREBLOW, G. J. THOMPSON, W. E. WASTE, JOSHUA HENDY IRON WORKS, a corporation, INTERNATIONAL ENGINEERING COMPANY, INC., a corporation, and MARINE TERMINALS CORPORATION, a corporation,
Respondents.

On Petition for a Writ of Certiorari to the Supreme Court of the State of California

Brief for Respondents in Opposition

MAX THELEN
ROBERT L. BRIDGES
111 Sutter Street
San Francisco 4, California

Attorneys for Respondents

THELEN, MARRIN, JOHNSON & BRIDGES
EDWARD J. RUFF
111 Sutter Street
San Francisco 4, California

Of Counsel

PARKER PRINTING COMPANY, 180 FIRST STREET, SAN FRANCISCO 5

SUBJECT INDEX

	Pages
Opinions Below	1
Jurisdiction and Restatement of Questions Presented	2-3
Statement of the Case	3-10
Argument	10-18
A. The Petition Should Be Denied Because the Federal Question Sought to Be Reviewed Was Not Properly Raised and Preserved in the State Courts as Indicated by the Certified Record	10-13
B. The Petition Should Be Denied Because the Judgment Is Based on Independent Non-Federal Grounds Adequate to Sustain It	13-16
C. The Petition Should Be Denied Because There Is No Substantial or Any Federal Question Which Exists	16-18
Conclusion	18

TABLE OF AUTHORITIES CITED

Cases	Pages
American Surety Co. v. Baldwin, 287 U.S. 156 (1932)	11, 14
Bailey v. Anderson, 326 U.S. 203 (1945)	14
Bradley v. Bradley, 94 C.A. 2d 310, 211 P.2d 638 (1949)	11
Brinkerhoff-Faris Trust & Savings Co. v. Hill, 281 U.S. 673 (1930)	13
Davenport v. Stratton, 24 C.2d 232, 149 P.2d 4 (1944)	10
Davidson v. New Orleans, 96 U.S. 97 (1877)	17
Edelman v. California, 344 U.S. 357 (1952)	10, 14
England v. Hospital of Good Samaritan, 14 C.2d 791, 97 P.2d 813 (1939)	13
Estate of Kent, 6 C.2d 154, 57 P.2d 901 (1936)	8
Fallbrook Irrigation District v. Bradley, 164 U.S. 112 (1896)	17
Gore v. Bingaman, 20 C.2d 118, 124 P.2d 17 (1942)	13
Gorman v. Washington University, 316 U.S. 98 (1942)	10
Gryger v. Burke, 334 U.S. 728 (1947)	17
Herb v. Pitcairn, 324 U.S. 117 (1945)	13
Herndon v. Georgia, 295 U.S. 441 (1935)	11
King v. West Virginia, 216 U.S. 92 (1910)	13
Martin v. Howe, 190 Cal. 187, 211 Pac. 453 (1922)	8
Missouri v. Gehner, 281 U.S. 313 (1930)	13
Moss v. Ramey, 239 U.S. 538 (1916)	13
Mutual Life Insurance Company v. McGrew, 188 U.S. 291 (1903)	10
Overton v. Vita-Food Corp., 94 C.A. 2d 367, 210 P.2d 757 (1941)	15
Prince v. Hill, 170 Cal. 192, 149 Pac. 578 (1915)	11

Pages

Radio Station WOW v. Johnson, 326 U.S. 120 (1945) 11, 14
Rice v. Sioux City Cemetery, 349 U.S. 70 (1954) 18

Sanders v. Howard Park Co., 86 C.A. 2d 721, 195 P.2d 898 (1948) 11
Saunders v. Shaw, 244 U.S. 317 (1917) 13
Southern Power Co. v. North Carolina Public Service Company, 263 U.S. 508 (1924) 15
Stembridge v. Georgia, 343 U.S. 541 (1951) 14

Tracy v. Ginzberg, 205 U.S. 170 (1907) 16

United States v. U. S. Smelting Co., 339 U.S. 186 (1950) 13

Wilson v. Loew's Incorporated, October Term 1957—No. 33, 26 L.W. 3248 13

STATUTES

California Insurance Code, Sec. 1101 5

United States Code, Title 28, Sec. 1257 10

In the Supreme Court of the United States

OCTOBER TERM, 1957

No. 801

G. W. THOMAS DRAYAGE & RIGGING COMPANY, INC., a corporation, W. R. BALLINGER & SON, a corporation, and MINNA M. BALLINGER,
Petitioners,

vs.

INDUSTRIAL INDEMNITY COMPANY, a corporation; INDUSTRIAL INDEMNITY EXCHANGE, a reciprocal exchange; T. G. McGUIRE, E. A. MATHIESSEN, S. E. HODAPP, J. V. CHAMBERS, M. S. FIELDS, E. E. URSIN, D. W. SCHIEBEL, W. A. HALUK, R. E. MAY, JR., R. L. JONES, JR., FRED DREXLER, N. S. YOUNG, THOMAS SOULE, J. P. TAHENY and V. E. HOWARD, JR., doing business as Industrial Service Company, a copartnership, HENRY J. KAISER, K. K. BECHTEL, S. D. BECHTEL, JOHN A. McCONE, W. A. BECHTEL, JR., T. G. McGUIRE, E. S. DULIN, F. SOMERS PETERSON, JAMES M. SMITH, M. I. SMITH, ALDEN G. ROACH, ROBERT L. BRIDGES, H. S. LORD, A. F. BISHOP, all of the aforesaid doing business as INDUSTRIAL UNDERWRITERS, a partnership, K. K. BECHTEL, L. T. KETT, F. SOMERS PETERSON, J. W. SCAMMELL, G. G. SHERWOOD, EMERSON SPEAR, A. G. STREBLOW, G. J. THOMPSON, W. E. WASTE, JOSHUA HENDY IRON WORKS, a corporation, INTERNATIONAL ENGINEERING COMPANY, INC., a corporation, and MARINE TERMINALS CORPORATION, a corporation,
Respondents.

On Petition for a Writ of Certiorari to the Supreme Court of the State of California

Brief for Respondents in Opposition

OPINIONS BELOW

Petitioners refer to a written opinion of the District Court of Appeal (App. C to Petition) which is unreported in the official California Appellate Reports, but which appeared in the interim Advance California Appellate

Reports at the time it was rendered. This opinion of the District Court of Appeal became a nullity when the Supreme Court of the State of California granted a petition for hearing in 1956 and thereafter was no more effective than if it had not been rendered, except as a brief on the questions discussed. (See Footnote 8, infra, p. 8)

JURISDICTION AND RESTATEMENT OF QUESTIONS PRESENTED

Does jurisdiction exist and will certiorari be granted to review the judgment of a state court of last resort when:

1) *The federal question,* if any, was not properly raised and preserved in the state courts. It seasonably could have been but was not raised before the trial court, before the District Court of Appeal, and before the Supreme Court. It *was first raised in the petition for rehearing to the State Supreme Court,* whose opinion had fully affirmed the earlier decision of the trial court. *This petition was denied without opinion.*

2) Assuming for the sake of argument the existence of a federal question the judgment of the California Supreme Court rests on an adequate non-federal ground, in that:

a) The federal question was never raised in the trial or appellate courts until the filing of a petition for rehearing in the State Supreme Court and under California rules of procedure an appellate court will not consider points which are not raised in the court below or in the original brief and points raised for the first time in a petition for rehearing come too late.

b) It *affirms* the earlier decision of the trial court, based on substantially unchallenged find-

ings of fact as made by that court, with regard to the uncomplicated question of ownership of certain property upon the same principles of local and general law which had been urged throughout the litigation and without any consideration or discussion of any federal question.

3) No substantial or any federal question is presented since the judgment of the state court is solely concerned with a determination of controverted substantive questions of ownership of property based upon the particular individual facts of the instant case and under principles of local and general law, with full opportunity having been afforded to all parties in interest to be heard before every court in the state judicial system having any jurisdiction.

STATEMENT OF THE CASE

The principal respondents in this case are Industrial Indemnity Company, a stock company (hereinafter called Company), engaged in the casualty and workmen's compensation insurance business; Industrial Indemnity Exchange (hereinafter called Exchange), a reciprocal insurance exchange which was engaged in the workmen's compensation insurance business until 1949; and Industrial Underwriters, a partnership (hereinafter called Underwriters) which managed the Exchange as Attorney in Fact under the provisions of an Underwriters Agreement. The petitioners are former holders of policies of insurance issued by Exchange.

Certain pertinent facts which were overlooked or misstated in the petition should be emphasized.

Contrary to petitioners' statements (Brief, p. 6) of competition and diversion of business, the fact is that "there

was considerable interrelation between Exchange and Company but *no* competition." (Emphasis ours.) (App. A to Petition, 49 A.C. 259)[1] "Company has *never* been operated in competition with Exchange." (Emphasis ours.) (App. B to Petition, 117 C.A. 2d 537)[2]

With regard to the 1947-8 objections made by the Insurance Commissioner which led to the Transfer and Assumption Agreement the court found "The attorney and the Company—maintained that all they had done was proper under existing law, agreements and circumstances (their said position was later generally sustained in the findings herein)." (App. B to Petition, 117 C.A. 2d 524) It should also be noted that Underwriters decided in December, 1948 that no further policies would be issued in the Exchange (C.T. 73, Finding XII).[3] In this respect the court found that Underwriters had no obligation to issue any further policies, had the power to cancel all policies and liquidate subscribers' accounts and as Attorney in Fact could not be replaced by the subscribers (C.T. 72, 73, Finding XI). Since December 31, 1948 Exchange has been engaged in no business except for liquidation (C.T. 73, Finding XII). The execution of this Transfer and Assumption Agreement between Company and Exchange was approved by the Insurance Commissioner and 98% of the then subscribers of the Exchange (App. B to Petition, 117 C.A. 2d 525).

---

(1) The reference "App. A to Petition" is to the decision of the Supreme Court of California (49 A.C. 257, 316 P.2d 966) to which the petition is directed, and the page references are to that decision as it appears in Appendix A to the Petition and as they appear in 49 A.C. 257.

(2) The reference "App. B to Petition" is to the first decision of the District Court of Appeal in 1953 (117 C.A. 2d 519, 256 P.2d 677) and the page references are to the decision as it appears in Appendix B to the Petition and as they appear in 117 C.A. 2d 519.

(3) The reference "C.T." is to the pages of the certified record constituting the Clerk's transcript. The reference "R" is to the pages of the certified record constituting the reporter's transcript.

With regard to the appeal after the first trial in 1950, it should be emphasized that the District Court of Appeal, *on its own motion* and without it having been previously suggested by any of the parties or the Insurance Commissioner, raised the question of the applicability of Section 1101 of the California Insurance Code to this agreement and held that, irrespective of good faith of the parties,[4] the approval of the Insurance Commisioner and 98% of the subscribers, the agreement was illegal and void under this Section as *then* written.[5] The Appellate Court, however, affirmed the decision of the trial court that cross-complainants (petitioners here) had no claim to the separate business of the Company. The Appellate Court then reversed the judgment and issued its remittitur with the very significant directions that the action for declaratory relief concerning the illegal agreement must be dismissed, and "as in the cross-actions, relief will be granted only with respect to the consequences of the illegality of the transfer and assumption agreement," (App. B to Petition, 117 C.A. 2d 540), the trial court shall grant cross-complainants "such relief as the court will deem fit to enable them to recover in their representative capacity for subscribers the business and assets obtained by Company in consequence of

---

(4) In the concurring opinion of Justice Schauer in the Supreme Court in 1957, he notes, with reference to the decision of the District Court of Appeal in 1953, "the good faith of respondents, already conclusively shown." (App. A to Petition, 49 A.C. 275-276)

(5) The California Legislature amended Section 1101 of the Insurance Code in 1955 so that "such an agreement as that which gave rise to the current controversy may now be legally made and performed, thus indicating that no basic principle of public policy, fairness or justice was violated when it was executed in 1948" (App. A to Petition, 49 A.C. 277). It is apparent that because of the statutory amendment the peculiar questions of this case will not arise again and the results of this case can have no effect on the public or other litigants.

the agreement herein held to be invalid." (App. B to Petition, 117 C.A. 2d 540-541)[6]

Petitioners also neglect to point out that Company, following this decision, on November 4, 1953 transferred all business and assets of the Exchange then in its possession back to Underwriters as Attorney-in-Fact for Exchange, who had been granted by the Insurance Commissioner a certificate *for the purpose of conducting liquidation* of the Exchange and Underwriters accepted these funds and has since been acting in liquidation of the Exchange (C.T. 67-68, Finding III).

The Superior Court, pursuant to the remittitur issued by the Appellate Court (C.T. 1, 2), and on the basis of pleadings filed by all parties, tried and determined the issue of what business and assets of Exchange were obtained by Company in consequence of the illegal agreement. It should be particularly noted that the trial court specifically found, on the basis of all evidence introduced, that the business and assets were of a value of $323,300.84[7] and had been returned

---

(6) It is apparent that the issue, of *what* business and assets Company had obtained from Exchange *in consequence of the invalidity of the agreement* and must be restored, had not been before or decided by the first trial court and was not necessary to the decision of the Appellate Court or decided by it. Thus there was not and could have been no law of the case on this point and this was the issue to be determined by the trial court on remand. This is expressly stated in the vacated decision of the District Court of Appeal in 1956 where the court states that its former opinion did "no more than to direct that appellants be allowed *whatever* recovery they might be entitled to in equity for the wrongful taking over of the business of the Exchange. *We did not consider, much less decide, the extent and nature of that relief*" (Emphasis ours—App. C. to Petition, p. 256). The Supreme Court in its decision expressly holds that "In view of the former decision on appeal the trial court was limited to a determination of this issue: What business and assets were obtained by Company in consequence of the 'Transfer and Assumption Agreement'?" (App. A to Petition, 49 A.C. 261)

(7) Under the contractual provisions of the illegal Transfer and Assumption Agreement, which had been declared void and could

by Company to Exchange, that prior to December 31, 1948 Underwriters had determined to issue no new policies in Exchange and that since December 31, 1948 Exchange has been engaged in no business except for liquidation, and that the business and assets of Exchange did *not* include either the items of Special Surplus or Attorney-in-Fact Fees (since these were exclusively the property of the Attorney-in-Fact under the particular facts of this case and the terms of the Underwriters Agreement. C.T. 70-73, 76, 77; Findings VII, VIII, IX, X, XII, XXI, XXV, XXVI) or profit earned by Company on insurance policies placed with Company after December 31, 1948 by former policyholders of Exchange (since the facts disclosed that these policies were not placed with Company as a consequence of the illegal agreement but as new voluntary, and independent pieces of business. C.T. 68-69, 72-75, 76-77, 78; Findings IV, V, XI,

---

not therefore be performed, the subscribers would have received $1,018,589.07 (C.T. 67, Finding II). This figure was not, however, the true liquidating net worth of the Exchange but an adjusted net worth increased by concessions of Company and Underwriters and, contrary to petitioner's assertion (Brief, p. 8, 21), was not an amount which had been stipulated between the parties as being the value of the business and assets of the Exchange. The reason for the much lesser amount under the Court's judgment is that a) the Attorney-in-Fact had as a part of the illegal agreement waived its right to the Special Surplus, in the sum of $592,322.31, to which it was otherwise entitled under the terms of the Underwriters Agreement "in the event Exchange discontinues business—to defray expenses of and as compensation for liquidation" (C.T. 71, 72, Findings IX and X) and to which the Attorney reasserted its right after the finding of illegality and b) Company had, under the illegal agreement, agreed to absorb losses, if any, on policies then in force which it reinsured and these policies developed a loss of $156,600.53 (C.T. 69, Finding VI), which losses were for the account of the Exchange after the finding of illegality. The effect of the illegality and unenforceability of the agreement was to deprive the Exchange of these benefits. It should however be noted that, irrespective of this legal result, K. K. Bechtel, the president of Company, affirmed its intention to see that the subscribers in fact received whatever would have come to them under the technically illegal agreement, less costs of litigation (App. A to Petition, 49 A.C. 275).

XII, XIII, XIV, XV, XVI, XVII, XXII, XXX). The items of Special Surplus, Attorney in Fact fees and profit on Company policies were the additional items claimed by petitioners as part of Exchange business and assets. *No issue of due process or equal protection was raised at any time before the trial court.*

Petitioners then appealed and the District Court of Appeal reversed the judgment of the trial court. Contrary to the statement at p. 13 of the petition, this decision makes no mention of any law of the case stemming from its earlier decision as being controlling and as not having been followed by the Trial Court or disregarded by the Trial Court and states that it had not considered, much less decided, the nature and extent of relief. (See Footnote 6, *supra*, p. 6). *No issue of due process or equal protection was raised at any time before the District Court of Appeal.*

A petition for hearing was then granted by the Supreme Court of the State of California.[8] *No issue of due process or equal protection was raised at any time in these proceedings before the Supreme Court.*

The Supreme Court by majority opinion *affirmed* the judgment of the Trial Court on the principle that "It logically follows that since the trial court's findings are supported by evidence and covered the issues the Appellate Court had ordered retried, the judgment in the principal

---

(8) Under California rules of procedure it is the unquestioned rule that the granting by the Supreme Court of a petition for hearing effectively nullifies the decision of the District Court of Appeal which ceases to have any effect except as a brief on the questions discussed, and the case is at large to be decided as if originally appealed to the Supreme Court. *Estate of Kent*, 6 C.2d 154, 156, 57 P.2d 901, 902 (1936); *Martin v. Howe*, 190 Cal. 187, 188, 211 Pac. 453, 454 (1922). The effect of this rule, contrary to petitioners' assertions (Brief, p. 14), is that petitioners here were appellants before the Supreme Court just as effectively as if they had appealed there directly (e.g. see the title of their Petition for Rehearing).

amount should be affirmed" (App. A to Petition, p. 266). The court observed that appellants (petitioners here) did "not attack these findings on the ground of insufficiency of the evidence" (App. A to Petition, p. 266), that "the evidence amply supports the finding, that future profits, Attorney Fees and the Special Surplus Fund were not items obtained by Company as a consequence of the illegal Transfer and Assumption Agreement" (App. A to Petition, p. 271-272), that "the foregoing findings, which are not disputed, show that • • • policyholders have not been injured by the execution of the Transfer and Assumption Agreement, and that they have received all to which they are entitled. Therefore, they have not suffered either injury or damage" (App. A to Petition, p. 272), and that "Company has not been unjustly or unfairly enriched" (App. A to Petition, p. 273).

Contrary to inferences (Petition, p. 22) of complete disagreement in the Supreme Court, Chief Justice Gibson, in a dissent concurred in by Justice Traynor, agreed that the law of the case was simply "that the subscribers are entitled to recover the business and assets obtained by Company as a consequence of that agreement" (App. A to Petition, p. 277-278); agreed that "there is sufficient evidence to support the trial court's finding that the business profits were not obtained as a consequence of the void Transfer and Assumption Agreement" (App. A to Petition, p. 279); but felt that as to the Attorney-in-Fact Fees and Special Surplus only issues of law based on undisputed facts were presented and that the conclusion of the trial court and the majority of the Supreme Court on these points was erroneous. It was only Justice Carter, in a separate dissent, who disagreed with everyone else.

Then followed the *petition for rehearing. Here for the first time in the 10-year history of the litigation* (which had

involved two trials on the merits and three appeals), *petitioners raised the question of due process and equal protection.* In the answer to the petition for rehearing it was argued, among other things, that under California law this point came too late (Answer to Petition for Rehearing, p. 9). *This petition was summarily denied by the court without opinion.*

ARGUMENT

A. The Petition Should Be Denied Because the Federal Question Sought to Be Reviewed Was Not Properly Raised and Preserved in the State Courts as Indicated by the Certified Record.

It is the unquestioned rule that before certiorari can or will be granted it is petitioners' burden to show affirmatively that the Supreme Court has jurisdiction (*Gorman v. Washington University,* 316 U.S. 98, 101 (1942)). Since jurisdiction here is allegedly based upon subparagraph (3) of Section 1257 U.S.C. Title 28, it must appear that the federal question has been "specially set up or claimed." In this respect it is clear that the court is without power to decide whether constitutional rights have been violated when the federal questions are not seasonably raised in accordance with the requirements of state law (*Edelman v. California,* 344 U.S. 357, 358 (1952)).

Under the California rules of procedure appellate courts will not consider contentions which have not been made in the trial court or lower appellate courts, or in the original briefs filed in the Appellate Court. [*Mutual Life Insurance Company v. McGrew,* 188 U.S. 291, 309 (1903) and California cases therein cited: *Davenport v. Stratton,* 24 C.2d 232, 242, 243, 149 P.2d 4, 9 (1944)]. It is admitted by petitioners in this case, and apparent from the record, that the federal questions of due process and equal protection were not raised in the trial court, were not raised before the District

Court of Appeal, and were not raised before the Supreme Court prior to its final decision (Petitioner's Brief, pp. 17 and 34).

The question was raised for the first time before the California Supreme Court in a petition for rehearing which was summarily denied without opinion (Petition, p. 2). Nothing is better settled than the proposition that a federal question comes too late when raised for the first time in a petition for rehearing, unless the court passes on the question so raised. [*Radio Station WOW v. Johnson,* 326 U.S. 120, 128 (1945); *American Surety Co. v. Baldwin,* 287 U.S. 156, 163 (1932); *Herndon v. Georgia,* 295 U.S. 441, 443 (1935)]. This rule is in accordance with the procedural rule followed in California to the effect that "an argument based upon a point not mentioned in the original brief of the petitioner will be of no avail on its demand for a rehearing. The judgments of appellate courts will not be upset in order to grant a rehearing unless the basis of the petitioners' demand was presented in his opening brief." [*Sanders v. Howard Park Co.,* 86 C.A. 2d 721, 723, 195 P.2d 898, 899 (1948); see also *Prince v. Hill,* 170 Cal. 192, 195, 149 Pac. 578, 580 (1915); *Bradley v. Bradley,* 94 C.A. 2d 310, 312, 211 P.2d 638 (1949)].

We are not concerned here with a situation where the Supreme Court acted upon the petition for rehearing and made a decision on the point raised, since the petition for rehearing was denied without opinion.

Petitioners attempt to avoid the necessary result of these rules of law by claiming "surprise" upon the basis that they had no reason to anticipate that the Supreme Court would affirm the judgment of the trial court and that the federal question was created by the decision of the Supreme Court which petitioners had not expected. This statement on its

face is ridiculous. If the federal question arose at all it necessarily arose at the latest when the Superior Court entered its judgment in 1955. It was at that time that petitioners must necessarily have been aware that their views of the case were not being followed and if there was any federal question involved it should have been raised at that time. This could have been done in a motion for new trial before the court which tried the case. It could thereafter have been raised in the course of petitioners' appeal to the District Court of Appeal, in petitioners' answer to the petition for hearing by the Supreme Court and it could have been raised as a last resort in the two oral arguments before the Supreme Court.

An unrealized hope or belief of petitioners that the ultimate result would be different when the case was finally brought to and decided by the Supreme Court is no surprise. The contention that petitioners expected that the Supreme Court would follow an earlier decision of the District Court of Appeal which, according to petitioners' views, established a certain law of the case completely overlooks the fact that the trial court failed to follow petitioners' views. It was at that time that the die was cast. It is impossible to see how a person can be surprised by an ultimate appellate decision which affirms a trial court's decision upon the same grounds which have been urged throughout the proceeding.[9]

---

(9) Petitioners claim at page 33 of their Brief that the rule of law of the case was binding upon the California Supreme Court. The petitioners' beliefs as to what constituted the law of the case are directly controverted by the District Court of Appeal and the Supreme Court (see Footnote 6, *supra*, p. 6). Assuming for the sake of argument that petitioners' beliefs in this respect were correct, the fact still remains that in California an appellate court is not absolutely precluded by law of the case from reconsidering earlier questions—the notion of limited power has been rejected and the courts treat the doctrine as one of policy and discretion. It is a

This is not a situation falling within the principle of the surprise cases. There was here ample opportunity to earlier present the objection and in fact imperative notice by the trial court's decision that it should be presented. This is not a case where the federal claim arose from the unanticipated disposition of the case at close of proceedings in the State Supreme Court (e.g. *Saunders v. Shaw,* 244 U.S. 317, 320 [1917]) nor is the federal claim based upon an unanticipated act of the Supreme Court in giving a new construction to a statute (e.g. *Missouri v. Gehner,* 281 U.S. 313, 320 [1930])or a situation where an unanticipated reversal of prior decisions concerning procedure left the claimant without relief (e.g. *Brinkerhoff-Faris Trust & Savings Co. v. Hill,* 281 U.S. 673, 677 [1930]).

B. The Petition Should Be Denied Because the Judgment Is Based on Independent Non-Federal Grounds Adequate to Sustain It

There are in this case two independent non-federal grounds, either of them being adequate to sustain the judgment. In such a case certiorari should be denied. [*Wilson v. Loew's Incorporated,* October Term 1957—No. 33, 26 L.W. 3248; *Herb v. Pitcairn,* 324 U.S. 117, 124, 126 (1945)].

1) The first of these is that the federal questions not having been seasonably raised in accordance with the requirements of state law, noncompliance with such local law is an adequate state ground for the decision below

---

mere rule of procedure and not one of substance. *England v. Hospital of Good Samaritan,* 14 C.2d 791, 795, 97 P.2d 813, 814, 815 (1939); *Gore v. Bingaman,* 20 C.2d 118, 122, 124 P.2d 17, 20 (1942). This is also the Federal rule (*U.S. v. U. S. Smelting Co.,* 339 U.S. 186 at 199 (1950). As a consequence it is clear that "there is nothing in the Constitution of the United States * * * to prevent a State from allowing past action to be modified while a case remains in court." This is so because the rule of law of the case "expresses only the practice of courts generally to refuse to reopen what has been decided, not a limit to their power". *King v. West Virginia,* 216 U.S. 92, 100-101 (1910). See also *Moss v. Ramey,* 239 U.S. 538, 546, 547 (1916) to the same effect.

[*Edelman v. California, supra,* 344 U.S. 357, 358 (1952); *Radio Station WOW v. Johnson,* 326 U.S. 120, 128, 129 (1945)]. It has been pointed out that under California rules of procedure (*supra,* pp. 10, 11) a point which has not been raised in the courts below or in the opening brief before the Supreme Court will not be considered by the Supreme Court on a petition for rehearing. The federal question here urged was concededly not raised until the petition for rehearing. The Supreme Court did not render any decision on the petition for rehearing and denied it summarily. It is clear that in this situation "the federal claim there made cannot serve as a basis for review by this Court" (*American Surety Co. v. Baldwin,* 287 U.S. 156, 163 (1932)).

The Supreme Court of California could have denied the petition for rehearing on the basis of the state rule of procedure that new points raised at this time come too late, but rendered no opinion. It is the unquestioned rule that where, as here, the highest court of the state delivers no opinion in denying the petition for rehearing and it appears, as here, that the judgment *might* have rested upon a nonfederal ground the Supreme Court will not take jurisdiction to review the judgment (*Stembridge v. Georgia,* 343 U.S. 541, 547 (1951)). Such an order of summary denial cannot be taken as a *decision* on a federal question presented in the petition; especially is this so where such a presentation is too late under state rules and could have been denied on that non-federal ground. [*Bailey v. Anderson,* 326 U.S. 203, 206, 207 (1945)]

2) The second independent nonfederal ground adequate to sustain the judgment sought to be reviewed is that judgment went against petitioners because the court found as a matter of state law that the basic and uncomplicated issue presented for determination was what property belonged to

petitioners, then found that the findings of the trial court in this respect were fully supported by the evidence and covered all of the issues to be tried, and therefore held that the judgment should be affirmed (*supra*, pp. 8, 9).

A question of ownership of property is necessarily a question of fact and construction of the contracts and relationships existing in the particular case in the light of those facts. The determination of those facts is for the trial court and they will not be disturbed except upon a showing that the findings of the trial court are unsupported by the evidence. In the absence of such a showing the findings are binding on the reviewing court, whose "power begins and ends with a determination as to whether there is any substantial evidence to support them" (*Overton v. Vita-Food Corp.*, 94 C.A. 2d 367, 370, 210 P.2d 757, 759 (1941)). Petitioners were afforded full, complete and adequate opportunity to present their views in every court having any jurisdiction of the matter. The decision of the Supreme Court was therefore based upon settled and established state principles of law which govern appellate courts in reviewing judgments of the trial courts. In short, there was no showing by petitioners that the items which they claimed were in fact their property and no showing that any of these items were a part of the business or assets obtained by Company in consequence of the illegal agreement.

The decision was obviously based upon the principle that before a person can claim property he must show that it belongs to him and since the facts, as established in the findings of the trial court and affirmed by the Supreme Court, are to the contrary neither injury nor wrong existed. Situations of this type—primarily factual—do not furnish grounds for granting certiorari [*Southern Power Co. v. North Carolina Public Service Company*, 263 U.S. 508, 509 (1924)].

CD1848

MATTHEW BENDER & COMPANY

MB

5-7

MICROCARD

TRADE MARK ®

Petitioners' contention that the decision of the Supreme Court of California was so grossly mistaken as to be impossible can only be applicable if it is assumed that the items claimed by the petitioners were in fact their property and a part of the business and assets. Since, however, as the decision clearly points out, the facts are to the contrary the argument begs the question. Petitioners' contention that the action was arbitrary completely overlooks and ignores the actual facts as found and the complete and full opportunities afforded for hearing before all courts having jurisdiction.

C. The Petition Should Be Denied Because There Is No Substantial or Any Federal Question Which Exists

Even if we are to assume that the decision of the Supreme Court of California was wholly erroneous in its determination of the ownership interests of petitioners, no question under the Fourteenth Amendment arises. Petitioners had full notice and opportunity to be heard and all actions were taken in accordance with the state's ordinary and regular procedure. The court, proceeding entirely upon principles of general and local law and giving all parties interested in the question an opportunity to be heard, decided that petitioners had no right to and did not own the items which they claimed.

> "The decision of a state court, involving nothing more than the ownership of property, with all parties in interest before it cannot be regarded by the unsuccessful party as a deprivation of property without due process of law, simply because its effect is to deny his claim to all such property. * * * the Fourteenth Amendment did not impair the authority of the states, by their judicial tribunals, and according to our settled usages and established modes of procedure, to determine finally, for the parties before it, controverted questions as to the ownership of property, * * *."
> [*Tracy v. Ginzberg*, 205 U.S. 170, 178 (1907)]

As is further pointed out in the case just cited, the opposite view would mean that "every judgment of a state court, involving merely the ownership of property, could be brought here for review * * * a result not to be thought of." [See, also, *Gryger v. Burke,* 334 U.S. 728, 731 (1947)]

It is a settled principle of law that a state court decision following its settled rules and in its regular course of procedure cannot be said to deprive a party of due process or deny him equal protection. The Supreme Court is not intended to be an appellate court for every unsuccessful litigant in a state court who questions the jurisdiction or the merits of a decision against him. If he has been afforded a fair trial according to applicable modes of procedure which do not involve a right secured by the Federal Constitution or an Act of Congress or Treaty then it is not possible to hold that he has, without due process of law, been deprived of his property. [*Davidson v. New Orleans,* 96 U.S. 97, 104 (1877); *Fallbrook Irrigation District v. Bradley,* 164 U.S. 112, 157 (1896)]

There is no Federal law, treaty or constitutionally secured right which is in question, nor is there any claim of repugnance of state statute to the Federal Constitution, Treaties or Laws. The case does not involve action under a state statute or regulation or municipal ordinance, such as was the situation in all of the cases cited at pp. 18-19 of the Petition. It is a simple case of a litigant who, after a full and complete hearing and final determination of the extent of his property ownership, received less than he wanted.

It should also be noted that the situation here involved is not possible of recurrence since the statute which gave rise to the dispute has been amended so as to now permit the legal making and performance of an agreement such as that which gave rise to this current controversy (see Foot-

note 5, *supra,* p. 5). Before this court will take jurisdiction it must appear that the federal question is one of substance. This court does not sit for the benefit of particular litigants [*Rice v. Sioux City Cemetery,* 349 U.S. 70, 74 (1954)]. It is apparent that the "episodic" situation in the instant case will be of no importance beyond the particular facts and parties involved.

Petitioners' claim of denial of equal protection (Petition, p. 31) on the basis of discrimination by a taking of property without compensation for the benefit of another and refusal to permit petitioners to retrieve property wrongfully obtained when other persons are permitted to do so, again begs the entire question at issue in the courts below which was: What property did belong to petitioners? The claim of denial of equal protection by alleged arbitrary refusal to apply the settled law of the state (Petition, p. 32) begs the same question since particular principles of general trust and fiduciary law can only be applied to facts as they exist in a particular case, and in the instant case the facts as established precluded the application of the principles contended for by petitioners.

CONCLUSION

For the foregoing reasons the petition for a writ of certiorari should be denied.

Respectfully submitted,

MAX THELEN
ROBERT L. BRIDGES
Attorneys for Respondents

THELEN, MARRIN, JOHNSON & BRIDGES
EDWARD J. RUFF
Of Counsel